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MARKETING AND DISTRIBUTION OF TOBACCO

Study prepared by the UNCTAD secretariat

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SCOPE OF THE STUDY AND MAIN FINDINGS

Scope of the study

(i) The present study sets out the factual background and examines the successive stages of the world tobacco economy from leaf production and processing through international marketing and shipping to production and distribution of tobacco products. In this context an attempt is made to study how these individual stages are linked. One of the main findings is that the seven large tobacco corporations or tobacco transnational conglomerates (TTCs) together effectively control each stage from leaf production in both developing and developed countries to the production and distribution of tobacco products on a worldwide scale.

(ii) The unit of analysis on which attention is focused is the tobacco transnational multiproduct conglomerate whose characteristics are product differentiation, size and increasing diversification which transcend national boundaries. The study examines the marketing structures within the wider socio-political and economic forces that have brought about the present pattern of the world tobacco industry. Accordingly, it goes beyond traditional marketing studies and conventional analysis whose central core is the fluctuations of supply and demand - a method wholly inadequate for any understanding of the worldwide operation of the oligopolistic powers of the TTCs. Moreover, in analysing the basis of the strength of the TTCs which lies in a combination of financial, technical, advertising, sales and marketing power, the approach of the study is multi-dimensional and extends beyond the boundaries of the specific commodity itself.

(iii) In order to understand the marketing and distribution structure of tobacco, and given the dominant role of the seven large tobacco corporations, it is necessary to study the growth over time of these corporations, and the nature of their participation in the marketing and distribution of tobacco. This the study attempts to do in some detail and in doing so highlights the formidable obstacles which the developing countries would have to overcome to move forward from the peripheral role to which they are at present confined in the marketing and distribution of tobacco and tobacco products. The main findings of the study are summarized in paragraphs (iv) - (xvii) below.

Growth of oligopolistic structures

(iv) The study examines the oligopolistic structures and their conglomerate manifestations in a historical perspective as far as globalization of output, marketing and distribution is concerned. Over time the tobacco oligopolistic structures, now highly product differentiated and self-reinforcing, on a national and global basis, have become more intricately enmeshed with, and geared to, other commodity sectors of the world market.

(v) The cumulative impact of economic concentration and the internationalization of capital has negated, in theory and in practice, the competitive market mechanism. Competition prevailed for only a very short time after the rise of the modern cigarette industry, giving way to a monopolistic phase between 1890 and 1911, and then to the present oligopolistic structures whose behavioural patterns are characterized by demarcation of market frontiers; specific modes of collusive conduct; price leadership and administered prices; and the continued shift in capital ownership from one national group to another.

Non-accountability

(xi) One of the salient features of TTC operations brought out in the study, in both the developed market-economy and the developing countries has been, and is, the absence of rigorous public accountability of their corporate practices, with the possible exception of the United States, stemming from the investigative activities of the Securities and Exchange Commission and the Anti-Trust Division of the United States Department of Justice. Disclosure and analysis are all the more vital since economic intelligence of such relevance is invariably shrouded in secrecy, strikingly so with respect to transfer pricing techniques. This is particularly evident in the developing countries, where knowledge of the financial, marketing and output decisions of the TTCs' global decision-making power is confined to rudimentary data, e.g. the conventional corporate balance sheet, which is largely stripped of any content. Data concealment is assisted by the giant accounting firms acting in alliance with corporate power. 1/ Deliberate withholding of information is seen in both developing and developed countries, notably in the former, since companies in the former colonies often operate under antiquated corporate law under which disclosure requirements are minimal.

Role of administered prices

(xii) Manifestation of oligopolistic power as exemplified in each and every phase of the tobacco economy indicates that pricing policy is determined not by perfect competition in competitive product and factor markets but by the fiat of administered prices. A seller-determined price is the salient trait of tobacco and cigarette market structures. Accordingly, a price theory based on marginal productivity theory loses all relevance as an analytical tool. It cannot be used to understand the mechanics of oligopolistic pricing policies and the capacity to control marketing power because its own premises include the absence of oligopoly and of market power wielded by a single firm. Any meaningful analysis must be based on a study of the many economic, social and political forces which determine the distribution of power.

Tobacco manufactured products

(xiii) Chapter III traces the extent of concentration in the marketing and distribution of tobacco manufactured products at the wholesale and retail level in the United Kingdom and the United States, and the operating margins at the wholesale and retail level, as well as the ramifications of the bootleg revolution in cigarettes in the United States. Special attention is given to the nature of non-price competition through restrictive contracts with retailers and through massive promotional expenditure. Although TTCs' competition is manifest, it is a specific form of competition only open to oligopolies with massive cash flows, and a competition which erects virtually insurmountable barriers to potential new entrants.

1/ Cf. United States Congress, Senate. The Accounting Establishment, prepared by the Subcommittee on Reports, Accounting and Management. 94th Congress, 2nd Session, Washington D.C., 1976.

(vi) World dominance of the TTCs and their expansionary upsurge was underpinned by their worldwide capital accumulation process, links with financial capital, mass advertising and the dynamics of cross-subsidisation.

Dominant role of the TTCs

(vii) At present, tobacco manufacturing in the developing countries and in the developed market-economy countries is largely dominated by seven large corporations or transnational tobacco conglomerates (TTCs): British American Tobacco, Imperial Tobacco Company, Philip Morris, R.J. Reynolds, Gulf and Western, the Rupert/Rembrandt/Rothmans Group and American Brands. Chapter II contains detailed case histories of these TTCs. Total sales of the big seven in 1976 were over $32 billion. Adding two lesser transnational tobacco conglomerates - Lorillard, a fully-owned subsidiary of Loews, and Reemtsma Cigaretten Fabriken GmbH in the Federal Republic of Germany - boosts aggregate sales of the world oligopoly to around $39 billion.

(viii) The power of the leading TTCs resides in their control of world cigarette manufacturing (accounting for about nine-tenths of all processed tobacco). Their direct operations account for more than 39 per cent of total world cigarette output. The balance is accounted for to the extent of 11 per cent by other private firms; 17 per cent by State tobacco monopolies in developed market-economy countries; and 33 per cent by State tobacco corporations in the socialist countries of Eastern Europe. Because TTCs are increasingly involved in licensing, selling and co-production relations with other firms, including State monopolies and producers in the socialist countries, the figure of 39 per cent seriously under-estimates the market shares of brands subject to their control. The existence of State monopolies is, in itself, no guarantee (notably within the framework of the European Economic Community) that the national market will remain invulnerable to the marketing encroachments of the TTCs, even in the absence of advertising. The Italian case history provides a good example, since one leading TTC brand alone accounts for about 30 per cent of total Italian consumption - licit and illicit.

Dynamics of cross-subsidization

(ix) TTCs have used their surplus cash flow to build up an intricate network of other activities related, in different ways, to the cigar-cigarette core of their business. Their resources now cover a whole range of manufacturing, mining, banking, insurance, shipping, communications, services, plantation and agricultural activities. Gulf and Western illustrates this trend toward broadening the scope of transnational activity in the reverse direction; it has diversified into tobacco.

Key role of advertising

(x) Global advertising costs of TTCs now amount to some $1.8 billion; their sheer magnitude can be gauged by the fact that the cost of launching a new brand has now risen to around $40 million. In addition to mass advertising, another integral component of world tobacco marketing is global corporate bribery or the "pay-off complex", involving millions of dollars.

Specialized tobacco machinery

(xiv) TTCs, notably BAT and Imperial, also dominate the production of the tobacco sector's specialized capital goods. Machinery required for leaf tobacco processing and manufacturing is dominated by three major transnational firms: Molins, Hauni, and American Machine and Foundry (AMF). Molins, a partially owned corporation of BAT and Imperial Tobacco, is the world's leader.

Pricing and marketing of leaf tobacco

(xv) Chapter IV deals with the pricing and marketing of leaf tobacco, through the auction system. Approximately 85-90 per cent of leaf tobacco that enters into international trade is under the direct or indirect control of about six transnational leaf buyers (see table 1). Some are TTC subsidiaries; and all are commercially linked with the TTCs much more than with leaf producers.

Marginal role of developing countries

(xvi) In such an economic framework of oligopolistic power, the developing countries are totally at the margin in the marketing decision process. Developing countries supply 55 per cent of world leaf tobacco through foreign oligopsony-controlled marketing channels; their processed exports are almost non-existent; they have no influence whatsoever in the design, output and innovation of machinery; their aggregate receipts from the tobacco industry are based, almost exclusively, on the demand response and marketing decisions determined, in the short, medium and long run, by the TTCs.

(xvii) The evolution of the political economy of tobacco is not unique. Its historic trends, dominance by a handful of TTCs and relegation of other economies, in particular the economies of developing countries, to uncertain, dependent activities under the TTCs' hegemony is common to a majority of the 24-odd commodities which dominate non-petroleum exports of the developing countries. Similarly, the TTCs are not unique, but typical in their effective creation of barriers to new entrants; active non-price competition with each other; generation of substantial surplus flows; cross-subsidization into new product lines and the building up of mutual self-reinforcing relations and with other transnational corporations.

(xviii) The progression of the tobacco transnationals to the privileged status they now enjoy has served to intensify the dependence of the developing countries on two major industrial centres. The bipolar relationships between the developing countries and the TTCs implanted in two industrial centres imply that there are no trade relations between developing countries, save those carried through the mediation of the tobacco transnationals.

(xix) A comprehensive, equitable and dynamic marketing and distribution framework remains to be devised that would permit the developing countries to assume a greater control of the industry. This, however, cannot be achieved exclusively within the framework of the tobacco industry; it must be integrated into more effective policies that would permit the comprehensive global regulation of the transnational corporations.

Table 1

Exports of developing countries marketed by transnational corporations, 1976

Commodity	Total exports ($ million)	Percentage marketed by transnationals
Food		
Cocoa	1 737	85
Bananas	793	70-75
Tobacco	1 079	85-90
Tea	827	85
Coffee	7 331	85-90
Sugar	4 801	60
Rice	1 102	70
Wheat	449	85-90
Agricultural raw materials		
Hides and skins	297 a/	25 a/
Natural rubber	2 202	70-75
Cotton	2 692	85-90
Jute	172	85-90
Forest products	4 169	90
Ores, minerals and metals		
Crude petroleum	29 149 a/	75 a/
Copper	3 031 a/	85-90 a/
Iron ore	1 256 a/	90-95 a/
Bauxite	518	90-95
Tin	604 a/	75-80 a/
Phosphates	850	50-60

Source: Estimates by the UNCTAD secretariat.

a/ 1973.

(xx) In the words of UNCTAD's Secretary-General, such a course becomes mandatory to overcome the constraints which the transnational corporations embody due to "an unprecedented concentration of financial power, technological know-how and productive capacity, which has enabled them to occupy a dominant position not only in the trade of developing countries but also in world trade in general". 2/

2/ New Directions and New Structures for Trade and Development. Report by the Secretary-General of UNCTAD to UNCTAD IV (TD/183/Rev.1) United Nations publication, Sales No. E.77.II.D.7., para. 22.

Chapter I

THE SETTING

1. Among some of the major problems and commodity policy issues to which the study addresses itself are: (a) The broad aims of TTCs' policy and to what extent, and why, they have led to the dominant position of these tobacco transnationals not only in developing countries but also in certain developed countries; (b) given that massive capital requirements, industrial and marketing technology and deepening links with finance capital have provided the dynamically linked strands of the tobacco industry, the likely future trajectory of the TTCs in the world tobacco industry both in the developed and in the developing countries; (c) the upper limits to cross-subsidization that has witnessed such a phenomenal growth over the last two decades, and which has gathered momentum over the last five years; (d) the repercussions of the extreme forms of mounting concentration on wholesalling and retailing of tobacco products; (e) whether the almost total domination of world tobacco exports and their shipment by the TTCs will continue. If so, what countervailing forces should be set in motion to reverse such pervasive control?

A. Methodology

2. At the outset, certain features of the analytical methodology employed need to be underlined. The unit of analysis on which attention is focused is the transnational multi-product tobacco conglomerate. It is qualitatively different from the "representative firm" conceptualized within a competitive structure. Where market power is diffused, all producers sell at an externally and objectively determined price, and price equilibrium is reached when marginal cost and marginal revenue are equal. In short an idealized competitive model which purported to explain what should have been happening theoretically but was not in fact happening historically.

3. In contrast to such an idealized competitive model, the TTCs, as is the case with all oligopolistic structures, do not sell at market determined prices what they decide to produce. As Professor Eichner has observed, the oligopoly sets a price, then produces and sells at that price whatever quantity the market will take; the price is thus seller-determined. 3/ It is the recognized interdependence of members of the oligopoly which determines their behavioural pattern. The implications of interdependence are that a given member of the oligopoly cannot modify prices unilaterally since such a course, were it to be pursued, would give rise to a serious price war, which would not necessarily lead to any changes in relative market shares. Hence "price leadership" implies that not only must pricing policies be co-ordinated, but also that the price, once agreed upon, must be sustained by its members until a further change is required by the oligopolists collectively.

3/ Alfred S. Eichner, The Megacorp and Oligopoly: Micro-Foundations of Macro-Dynamics, Cambridge University Press, 1976. He goes on to note that the tendency for an oligopolistic price to change infrequently is due to the fact that it is an administered price, with time required not only to co-ordinate the setting of a new price level, but also to evaluate the impact of the previous change in the price level.

4. Price leadership and administered or political prices which are its corollaries are shaped by specific configurations of economic power. The proliferation of cigarette brands by TTCs - one such configuration - far from being a manifestation of consumer sovereignty as it is rationalized to be, is a weapon deployed not only within the oligopoly but also for repelling potential new entrants by simply boosting the level of output required to break even, predicated as this is on a minimum market share. It thereby sustains an abnormally high level of corporate profitability, thus ensuring greater structural coherence. Reinforcing such oligopolistic exclusivism is the TTC's sheer size and product differentiation (non-tobacco) which transcend national frontiers.

5. In its world outlook the TTC, while firmly rooted in developed market-economy countries, conceives the world market as a single economic unit in which centralized planning of the enterprise becomes the ultimate and overriding concern to achieve global long-range profit maximization. 4/ Oligopolistic competition for ever larger market shares provides the dynamic for continuous growth through the integration of finance capital, industrial and marketing technology, transportation and consumer manipulation via advertising and promotional campaigns.

6. The essential strategy behind the accelerated dynamic for enhanced control resides in the movement of cross-subsidization 5/ involving the mass deployment of resources siphoned from one profit centre to acquire, ultimately, unfettered control over other industries. The increasing concentration of economic power - epitomized by the TTCs - is a crucial element in the world economy. Contributing to this exponential rate of economic concentration has been the wilting of national countervailing power, in both developed and developing economies, which might have been expected to inhibit the expansionary momentum. "When the system becomes global", write Barnet and Müller in terms applicable with particular force to the TTCs, "the parent company can shift profits through transfer pricing, 'profit loans swaps' and other accounting miracles on a wide scale, cross-subsidizing its various operations with the profits of others." 6/ These practices are well beyond the capabilities of smaller national firms.

7. In the case of TTCs, as is shown in detail in subsequent chapters, a centralized network of profit maximization and concentration of capital are endemic. Hence, at a certain point in time the individual profit centres and global corporate accumulation become mutually self-reinforcing. The intersecting configuration of these ramifying and self-reinforcing processes defines the co-ordinates of this study.

4/ Or in the formulation of Professor Milton Friedman examining the implications of that concept on business behaviour: "Few trends could so thoroughly undermine the very foundation of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for their stockholders as possible". Capitalism and Freedom, Chicago University Press, 1962, p. 133.

5/ For an analytical insight into the concept of cross-subsidization, see John Blair, Economic Concentration: Structure, Behaviour and Public Policy, New York, 1972.

6/ R.J. Barnet and R.E. Müller, Global reach: The power of the multinational corporations, New York, Simon and Schuster, 1974, pp. 255-256.

8. In the United States three conglomerates R.J. Reynolds, Philip Morris and BAT's subsidiary (Brown and Williamson) account for around 76 per cent of the cigarette market, with the first two having 33 per cent and 25 per cent respectively (see chart I). Gulf and Western (Consolidated Cigars) has around 25 per cent of the large cigar market and R.J. Reynolds almost 70 per cent of the small cigar market.

B. Market structure and the impetus to concentration

9. The meaning of market concentration used in this study is the overall concentration in tobacco manufacturing, that is, the relative shares of total tobacco manufacturing controlled by the leading conglomerates; concentration in specific product markets; and the range of dominance in tobacco markets centralized in the largest tobacco corporations.

10. The conceptual basis for analysis is the notion of market power on a global scale. This is analysed through the globalized profits accruing to, and the extent of concentration on, sales and assets under the control of the TTCs that define the modus operandi of the world tobacco economy.

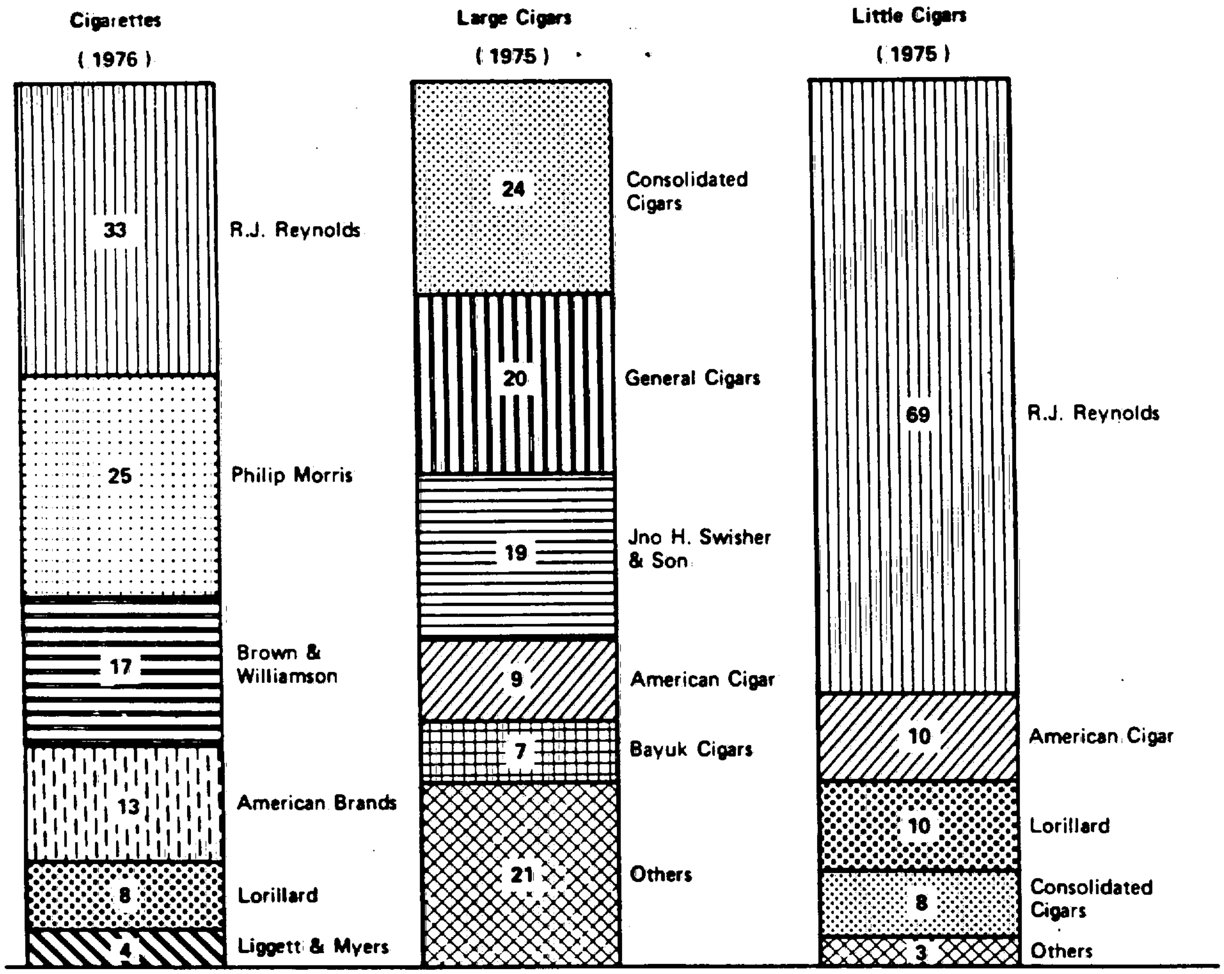
11. Although the TTCs are of relatively recent vintage, the "trust movement" at the turn of the century already highlighted the respective spheres of influence carved out by the Imperial Tobacco Company (ITC) and the American Tobacco Company (ATC), as well as their special creation: the British American Tobacco Company (BAT). By the turn of the century the two majors already ranked among the most highly capitalized industries in the Anglo-Saxon world (see table 2). Chapter II discusses the trend towards concentration of industry in the United States in the twentieth century.

12. Vertical integration in the United States reached its apotheosis with the Standard Oil Trust in which free and equal access to transportation was the decisive issue. "So long as it is possible", wrote Ida Tarbell at the conclusion of her study of the Standard Oil Trust, "to own the exclusive carrier on which a great natural product depends for transportation, and to use this carrier to limit a competitor's supply or to cut off entirely that supply if the rival is offensive, and to always make him pay a higher rate than it costs the owner, it is ignorance and folly to talk about constitutional amendments limiting trusts". 7/

7/ Ida M. Tarbell, The History of the Standard Oil Company, Gloucester, Mass, 1904 p. 283, quoted in M. Mintz and J. Cohen, Power Inc., New York, 1976, p. 237. All that has changed essentially, note these authors, since the early twentieth century, is that domination of the pipeline industry has passed from the Standard Oil Trust to joint ownership by the integrated majors, that is "from a monopoly to a shared monopoly". See also in the same marketing context, John M. Blair, The Control of Oil, New York, 1976 and Robert Engler, The Brotherhood of Oil: Energy Policy and The Public Interest, University of Chicago, 1977.

Chart I

US MARKET SHARES : CIGARS AND CIGARETTES
(in per cent)



Sources : Compiled from Business Week, Dec. 6, 1976; Consumer Services Reports; A tobacco Report 31 March 1975, and Maxwell International Estimates, 1975.

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Table 2

Ranking of industrial companies in the United Kingdom and United States, circa 1900

A. United Kingdom (1905)

Rank	Company	Industrial Group	Year of Registration	No. of Directors	Capitalization (£000)
1	ITC	Tobacco	1901	23	17 545
2	Watney, Combe Reid	Brewing	1898	10	14 950
3	J & P Coats	Textiles	1890	16	11 181
4	United Alkali	Chemicals	1890	16	8 490
5	Calico Printers Association	Textiles	1899	6	8 227
6	Vickers, Son & Maxim	Steel, ships and armaments	1897	15	7 440

B. United States (1895-1904)

Rank	Company	Per cent of market control	Capitalization ($ million)	Capitalization (£ 000)a/
1	US Steel	65	1 370	282 474
2	ATC	90	502	103 505
3	General Electric & Westinghouse	90	162	33 402
4	American Sugar Refining Co.	70-90	145	29 897
5	Distilling Co. of America	60	125	25 773
6	International Harvester	70	120	24 742

Source: P.L. Payne, "The Emergence of the Large Scale Companies in Great Britain, 1875-1914", Economic History Review, Vol. XX, No. 3, December 1967; R.L. Nelson, Merger Movements in American Industry, 1895-1956. Princeton University Press, 1959.

a/ Conversion rate: £1 = $4.85.

13. James Buchanan Duke (1857-1925), architect of the ATC, BAT's first Chairman of the Board and initiator of successive waves of consolidation, was to grasp rapidly the significance of vertical integration as pioneered by Standard Oil: "If John D. Rockefeller can do what he is doing in oil, why should I not do it in tobacco?" 8/ Indeed, Standard Oil provided the technical and inspirational and managerial blueprint for the build-up of ATC, and was represented on its board of directors.

14. The rise of the TTCs must be set against the change in national and global capital concentration that had taken place so rapidly over the last **eighty years**. It became a catalyst for the TTCs. Whereas there were only two or three giant (product-specialized) corporations with assets reaching $500 million in 1906, in the ensuing decades, size and diversification grew apace. In his United States Senate testimony on corporate growth and secrecy Professor Willard Mueller stated:

> "In contrast, by the first quarter of 1971, there were 111 industrial corporations with assets of $1 billion or more and nearly 200,000 partnerships and proprietorships engaged in manufacturing. These 111 corporations held at least 51 per cent of the assets and 56 per cent of the profits of all corporations engaged primarily in manufacturing; ...the 333 corporations with assets of $500 million or more accounted for fully 70 per cent of all industrial assets, excluding their unconsolidated holdings. Indeed, by 1970, the two largest industrial corporations alone had sales of nearly $40 billion, which is about as great (in constant dollars) as those of the over 200,000 manufacturing establishments operating in 1899." 9/

15. The picture in the United Kingdom is no less revealing. The largest 100 firms in terms of net output in manufacturing, which had accounted for a relatively stable share of manufacturing (22-24 per cent) between the early 1920s and the late 1940s, a share which had moved up to 27 per cent by 1953, saw their share spurt sharply, to slightly over 40 per cent, by 1970. The United Kingdom's industrial structure is already more concentrated than that of the United States. 10/

8/ The New York Times, 11 October 1925.

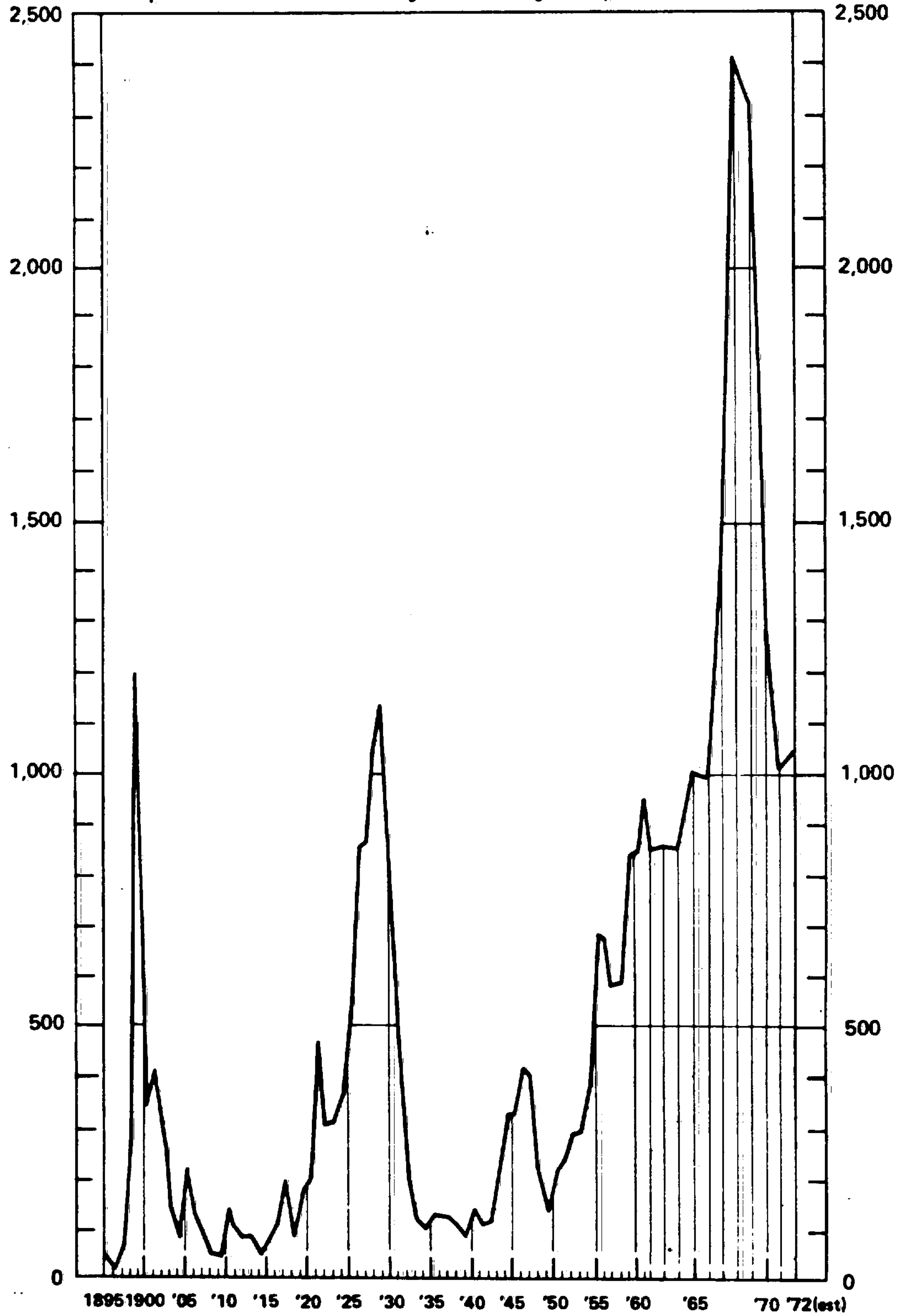
9/ United States Congress, Senate, Hearings before the Sub-Committee on Monopoly of the Select Committee on Small Business, The Role of Giant Corporations in the American and World Economies, Corporate Secrecy: Overviews. 92nd Congress, 1st Session, 9 and 12 November 1971, pt. 2: 1111. See also Federal Trade Commission Economic Report: Conglomerate Merger Performance. An Empirical Analysis of Nine Corporations. Washington, D.C. 1972.

10/ S.J. Prais, The Evolution of Giant Firms in Britain: A Study of the Growth of Concentration in Manufacturing Industry in Britain: 1909-1970, Cambridge University Press, 1976.

Chart II

U.S.A.

Acquisitions of Manufacturing and Mining Companies, 1895-1972



Source : Fortune, April 1973.

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16. Levels of concentration by size in the United Kingdom, measured by the shares of the enterprises in net manufacturing output, are shown in table 3. The data suggest that it is precisely those industries in which capital intensity and high advertising intensity go together which are the most concentrated. The highest degree of concentration (99.7 per cent in 1968) is that of the five tobacco enterprises. In reality, three enterprises alone accounted for over 92 per cent of sales. Also, the three heaviest levels of advertising - in soap, oils and fats, pharmaceuticals and tobacco (24.5, 17.9 and 17.1 per cent respectively of net output) - are roughly six times the average level for manufacturing enterprises; and except for pharmaceuticals the 1968 concentration level is almost a third higher than the overall average.

17. Summarizing the experience of the evolution of giant firms in the United Kingdom, whose relevance is particularly apposite to the global operations of the TTCs, Mr. Prais observes:

> "Advertising has played a complex part in the development of modern large-scale industry. High advertising and high concentration tend to go together, because advertising increases the size of the representative firm's market and hence (with a given total market) increases concentration; they also go together because in highly concentrated industries there is scope for heavy 'combative' advertising. Advertising is not an activity equally appropriate to all trades, but is particular to mass-consumable articles, where the heavy costs of an advertisement can be spread over a great many units. The hundred largest firms of today tend to be rather more active in such trades, and in the decade 1958-1968 it appears that giant firms have tended to move into such 'advertising-intensive' industries." 11/

18. Likewise, the mechanics of capital accumulation has produced the identical processes in the Federal Republic of Germany. According to the findings of the Federal Cartel Office there are similar levels of concentration in that country. 12/ Reemtsma, the largest tobacco manufacturer, in which the Reemtsma family owns 65 per cent of the firm's capital assets and which is one of the lesser TTCs, ranked thirtieth amongst the 100 largest enterprises by sales in 1974. The other two dominant enterprises, also included in the first 100, are BAT (rank 41), followed by Martin Brinkmann, a wholly owned subsidiary of Rothmans International (rank 51). Sales of those three TTCs account for 88 per cent of aggregate sales of the country's tobacco industry, and 2.5 per cent of all sales of the first 100 enterprises.

19. Dissolution of the American Tobacco Company in 1911 set the stage for the era of oligopolistic competition. The world spheres of influence agreement, consecrated on 27 September 1902, represented the grand climacteric of the Trust's activities. While the 1911 divestiture proceedings of the United States

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11/ *Ibid.*, p. 86.

12/ Federal Cartel Office, *Hauptgutachten 1973-1975. Mehr Wettbewerb ist Möglich*, Baden-Baden, 1976, and Commerzbank, *Wer gehört zu wem*, 11th edition, 1975.

Table 3

United Kingdom: Intensity of advertising, concentration, size of enterprise and multi-plant working

	Advertising a/ /net output	Concentration b/			Average size of enterprise		Plants per enterprise c/
					Employees a/	Net output	
	1963	1958	1963	1968	1963	1963	1963
	(%)	(%)	(%)	(%)		(£m.)	
High-advertising groups d/							
Soap, oils and fats	24.5	85.1	83.2	82.6	528	1.20	2.4
Pharmaceuticals and toilet preparations	17.9	35.6	34.5	38.3	716	1.36	2.1
Tobacco	17.1	98.5 e/	99.5	99.7	9 484	19.26	10.0
Cocoa, chocolate and sugar confectionery	11.3	53.9	65.5	69.5	1 448	1.77	2.5
Other food industries	11.0	77.8	83.1	82.4	960	1.39	4.0
Low-advertising groups							
Light metals, copper, brass, etc.	1.0	65.0	65.6	67.3	996	1.45	3.7
Cotton etc. spinning and weaving	1.0	27.8	37.3	49.4	643	0.53	3.3
Textile finishing	0.9	..	..	..	513	0.52	3.2
Coke ovens and mfd. fuels	0.8	61.9	65.3	98.6	472	0.71	1.3
Woollen and worsted	0.7	24.1	28.6	38.0	472	0.48	2.6
Insulated wires and cables	0.7	62.8	75.6	86.5 g/	2 542	3.48	4.0
Aircraft mfg. and repairing	0.5	89.8	97.5	99.4	4 793	6.12	4.1
Iron and steel	0.4	63.1	63.2	79.5 g/	1 968	2.74	4.3
Averages h/							
High-advertising	14.8	82.3	84.9	84.3	1 057	1.65	3.3
Low-advertising	0.6	55.4	58.0 i/	70.9 i/	1 311	1.36	3.4
All manufacturing	3.0	54.4 j/	58.8j/63.4k/	67.8 k/	882	1.20	3.2

Source: S.J. Prais, The Evolution of Giant Firms in Britain: A Study of the Growth of Concentration in Manufacturing Industry in Britain: 1909-1970, Cambridge University Press, 1976, p. 83.
The data are derived from censuses of production.

a/ For establishments of all sizes.

b/ Average share of sales of principal products of the group by five enterprises having largest sales of those products; shares of each product weighted by sales to form the average for the group.

c/ For enterprises with over a hundred employees; based on Census 1963, vol. 132, table 15, with interpolated estimates where figures suppressed to avoid infringement of disclosure rules.

d/ Product-groups for which advertising above 10 per cent of net output.

e/ Based on Hart, Utton and Walshe, 1973, p. 79.

f/ Product-groups for which advertising less than 1 per cent of net output.

g/ Not fully comparable with earlier years.

h/ Weighted by the denominators of the ratios in the respective columns.

i/ If insulated wires and cables, and iron and steel, where 1968 ratios not fully comparable, were omitted, these averages would be 45.4 (1958), 49.5 (1963) and 61.8 (1968).

j/ Relates to 214 product-groups comparable for 1958 and 1963.

k/ Relates to 295 product-groups comparable for 1963 and 1968.

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Department of Justice had ostensibly severed the monopolistic bonds of the ATC, there were important survivals. Singular in this respect were the explicit territorial demarcation lines between the Imperial Tobacco Company and BAT, manifested in their corporate interlocks of which the world's dominant tobacco engineering firm (Molins) is perhaps the most conspicuous. 13/ To this should be added the vital global role of their leaf tobacco marketing organizations.

20. By 1912 ATC's quasi-monopoly had blended into the oligopoly of the successor companies in which three corporations alone accounted for (in value) 76 per cent of chewing tobacco, 80 per cent of cigarettes and 76 per cent of smoking tobacco. 14/ Unwittingly, the divestiture proceedings which loosened the ATC-Imperial power complex bequeathed a legacy whose consequences were to be felt in the immediate years ahead, with BAT becoming the largest tobacco corporation in the world. BAT was to acquire untrammeled ascendancy in the British colonies, as well as in Latin America, which explains BAT's contemporary primacy in the developing countries - although this has been somewhat trimmed in recent years by the inroads of other members of the oligopoly.

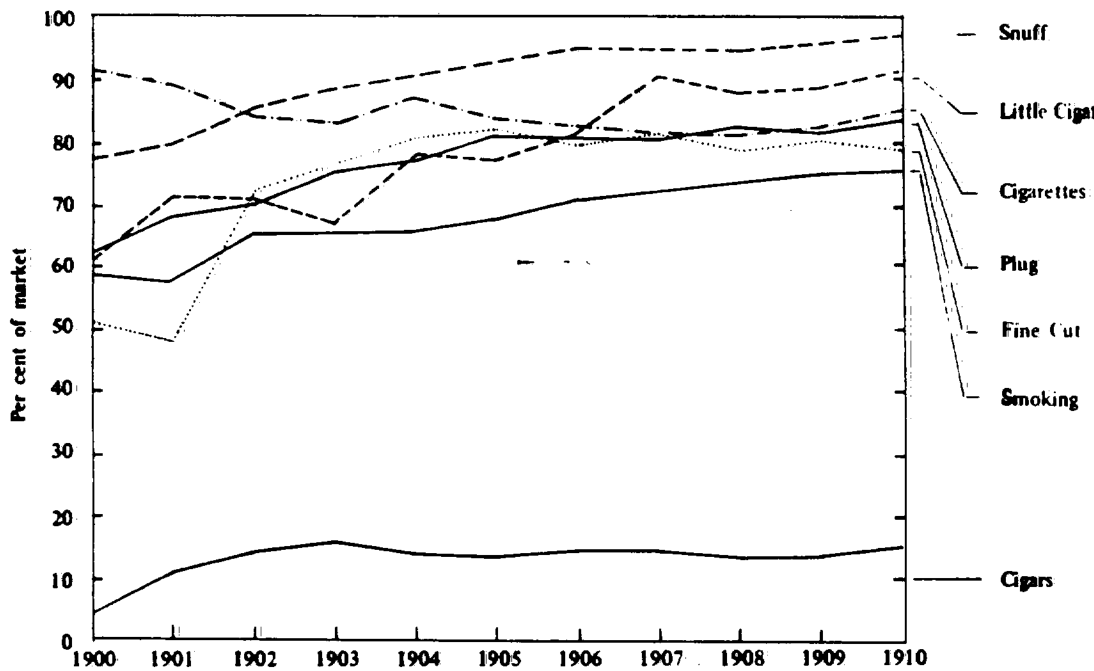
21. Movements in market shares in the United States since 1900 are illustrated in charts III and IV.

13/ Although the United Kingdom Monopolies Commission partially investigated in the 1950s certain aspects of the marketing practices of the Imperial Tobacco Company, no official investigation has ever scrutinized the confluence of political and economic power of Imperial and BAT.

14/ For a detailed picture see United States Bureau of Corporations, Report of the Commissioner of Corporations on the Tobacco Industry, Pts. I-III. Government Printing Office, Washington DC, 1911; Reavis Cox, Competition in the American Tobacco Industry, 1911-1932, Columbia University Press, 1933; N.M. Tilley, History of the R.J. Reynolds Tobacco Co., Commerce, Texas, 1976 (mimeo).

Chart III

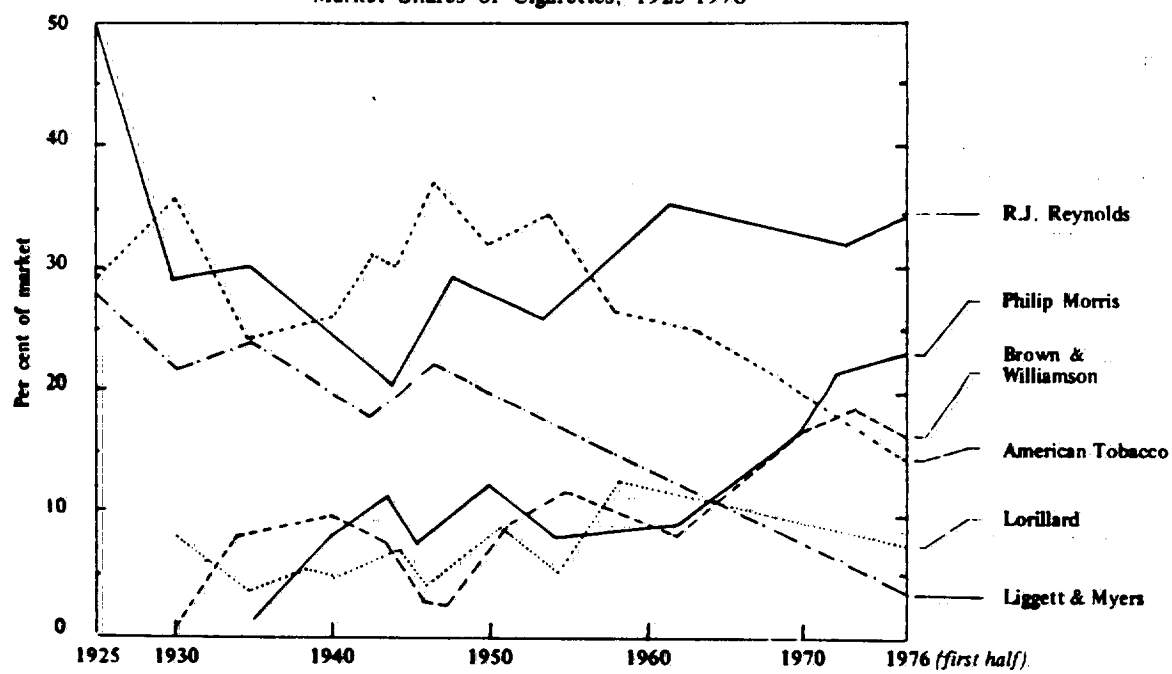
American Tobacco Company :
USA Market Shares, 1900-1910



Source: Report of the U.S. Commissioner of Corporations on the Tobacco Industry, Vol. III, Washington, DC 1915.

Chart IV

United States :
Market Shares of Cigarettes, 1925-1976



Source: Trade sources and Fortune, October 1976.

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22. Another feature of the impetus to concentration, as an OECD Committee of Experts has recently noted, is that firms sometimes "consolidate their economic power and draw advantages from it not only individually but also by means of agreements or concerted actions with other enterprises, particularly in oligopolies where most multinationals are to be found. Such agreements are facilitated by the possibility in many countries of legalizing certain types of cartels: for example, rebate, rationalization, import and specialisation cartels in which the subsidiaries of multinational firms may participate and which may, and in fact sometimes do, serve as the nucleus for an international system of restrictive agreements". 15/

23. Although the data are not sufficiently exhaustive, as the OECD experts further note, to assess precisely the role of export cartels on an industry by industry basis or to quantify exactly their economic significance, it can be concluded from the Federal Cartel Office that transnationals participate in around 70 per cent of all export cartels of the Federal Republic. In the United Kingdom an analysis of 41 international export cartels (32 per cent of all export cartels) showed that 20 out of 29 cartels with transnational participation had both British and foreign transnational members. 16/ United Kingdom experience, which is similar to that of the Federal Republic of Germany reveals that export cartels are pervasive in highly concentrated conglomerate oligopolistic structures, as indicated by the table below:

United Kingdom: Active Export Cartels and Industrial Concentration

5-Firm Concentration Ratio (per cent)	Number of Export Cartels
1 - 33	14
34 - 66	38
67 - 100	78
	130

Source: OECD, op.cit. citing P.D. Gribbin, Restrictive Business Practices, Multinational Companies and Trade with Developing Countries, New York, (mimeo) 1975.

24. It would therefore seem that there is a high incidence of transnational co-operation, particularly as regards their participation in export cartels. The following table also indicates the percentage frequency of restrictions

15/ OECD, Restrictive Business Practices of Multinational Enterprises: Report of the Committee of Experts on Restrictive Business Practices (Paris) 1977, para. 57.

16/ Ibid., para. 59.

found in 78 export cartels in the Federal Republic of Germany (39 national and 39 international.) Also noteworthy is the capability of the oligopoly in an international export cartel to induce other corporations engaged in domestic and foreign trade not to undermine the cartel's export prices. The data for the Federal Republic of Germany are themselves indicative in this respect:

Federal Republic of Germany: Percentage Frequency of Restrictions Found in Export Cartels (as of 31 December 1974)

	Price fixing	Fixing of rebates	Fixing of conditions	Fixing of quotas	Exclusive or preferential dealing	Ad hoc and/or collusive tendering	Open price systems	Pooling of profits	Joint ventures
International Export Cartels	76	18	67	59	13	8	28	21	13
National Export Cartels	15	5	76	31	-	21	28	8	15

Source: OECD, Restrictive Business Practices of Multinational Enterprises, (op cit.) p. 21

C. The paramount conglomerates

25. At present, tobacco manufacturing in the developing countries and the developed market-economy countries - apart from the State tobacco monopoly countries - is dominated by five large TTCs (British American Tobacco, Imperial, the Rembrandt/Rupert Group, R.J. Reynolds and Philip Morris) which straddle the globe with hundreds of proprietary brand names, and for which tobacco accounts for a diminishing share of their global output, sales and profits. To this should be added two lesser transnational conglomerates: Lorillard, a fully owned subsidiary of the Loews' Group and Reemtsma Cigaretten Fabriken, GmbH, a family-owned enterprise in the Federal Republic of Germany. The global oligopoly has more recently shrunk dramatically with the acquisition by BAT of the entire international operations of Lorillard for [illegible] million cash. This involves above all the take-over of prestige proprietary brands, including Kent.

26. The pace of conglomerate diversification can be seen from table 4, which shows the importance of non-tobacco returns to "tobacco" corporations. Conspicuous in having diversified into tobacco is Gulf and Western, whose share in the large cigar market is around 30 per cent in the United States (in addition to other overseas cigar interests), but which represented a mere 4 per cent of its returns in 1976. In the other direction the Liggett Group has diversified to the point that non-tobacco income substantially exceeded that from tobacco products by 1976.

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Table 4

Preparation of non-tobacco income of tobacco firms, 1971-1976

(Percentages)

	1976	1975	1974	1971
Liggett Group	61	59	56	53
Rothmans-Canada	52	54	60	64
Imperial Group	40	45	41	25
American Brands	27	30	29	32
British-American	26	23	30	7
R.J. Reynolds	25	27	30	25
Gallaher	21	35	25	12
Brown & Williamson	20	18	20	6
Imasco (BAT & ITC)	19	21	18	25
Rembrandt Group	15	11	10	-
Philip Morris	9	9	6	10
Loews a/	38	23	24	40
Gulf and Western a/	96	95	94	91

Source: Tobacco Reporter, December 1976

a/ Estimates by the UNCTAD secretariat based on data from the Tobacco Reporter

27. The drive to concentration in manufacturing is matched by an equally high incidence of concentration of leaf buyers, including some of the leading manufacturing corporations. In the United States four companies accounted for around 72 to 80 per cent of total auction purchases in 1976: Universal Tobacco Co. (25 per cent); Export Leaf, a totally owned BAT subsidiary (18 to 20 per cent); Dibrell Brothers (15 per cent); R.J. Reynolds (18 to 20 per cent).

28. On a global basis around 85 to 90 per cent of exports is accounted for directly or indirectly by eight transnational leaf purchasers, of which Universal Leaf is the world's leader. 17/ In Brazil, BAT's leaf-buying subsidiary controls and markets over 80 per cent of that country's leaf exports, an incidence of concentration that is matched by BAT's share of more than four-fifths of aggregate cigarette output in that country. The large transnational sellers are closely linked to the manufacturers through a panopoly of medium and long-term buying and selling contracts.

17/ See Chapter IV for an analysis of leaf tobacco marketing.

29. On a global basis, i.e. including the socialist countries of Eastern Europe (with most of which they have licensing agreements), these tobacco conglomerates account for some 39 per cent of aggregate cigarette output. In terms of world output excluding the tobacco State monopoly countries and the socialist countries of Eastern Europe, this percentage rises to 80 per cent. Through licensing agreements the figures of brand ownership are, of course, higher in both cases (see table 8).

30. Basic data on the seven TTCs are shown in tables 5 and 6 below. Four of them each have consolidated sales well in excess of $3 billion, with net incomes of more than $100 million and a labour force of more than 51,000. More recent data would reveal the sheer magnitude of marketing operations. Worldwide sales for the BAT group for the fiscal year ending 30 September 1976 were £5.4 billion ($9.2 billion) and profits £374 million ($640 million). 10/

31. Against this background of the dominant role of the TTCs it is not surprising that the developing countries have been relegated to the periphery of the marketing decision-making process.

32. The political economy of power will be studied in detail as seen in the analysis of the amplitude of conglomerate operations. There appears little scope for other producers to enter the global market for manufactured tobacco products. Allowing for the possibility of such intruders, they would be regarded as highly vulnerable to annexation or reduction of their (already highly circumscribed) freedom of manoeuvre due to the sheer weight of existing conglomerate power - with their actual and potential capacity for collective marketing sanctions - and their further ability to relate technology, finance capital and the communications media to attain their primary objective of ever larger market shares.

33. Recent evidence relating to the largest countries of the western hemisphere - Canada, Brazil, Mexico, Argentina and Venezuela - exhibits the extent of acquisition, although there are few, if any, countries which reveal such exclusive domination as BAT over its Sri Lanka manufacturing enclave. With the recent takeover of Macdonalds in Canada by Reynolds, the entire Canadian market is now subject to the decisions of three transnationals - Imasco, Reynolds and Rothmans,

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10/ The dollar conversion was made at prevailing exchange rates. (BAT Annual Report, 1976).

Table 5

Ranking of tobacco transnational corporations among the leading 500 industrial corporations of the United States, 1976 a/

Business indicator	R.J. Reynolds Industries	Gulf & Western Industries	Philip Morris	American Brands	Liggett & Meyers b/	Universal Leaf Tobacco
Sales ($ million)	4 291	3 395	3 134	2 671	719	706
Rank	41 (74)	57 (69)	65 (147)	80 (85)	283 (219)	290 (-)
Assets ($ million)	4 276	3 480	3 582	2 456	679	172
Rank	30 (68)	44 (34)	41 (108)	59 (52)	245 (161)	479 (-)
Net Income ($ million)	353	200	265	121	36	17
Rank	28 (27)	45 (77)	34 (107)	87 (49)	275 (205)	389 (-)
Stockholders' equity ($ million)	2 112	1 095	1 429	1 171	393	115
Rank	31	70	45	60	215	444
Employees	37 296	110 000	51 000	54 800	6 800	12 300
Rank	105	19	66	53	421	310
Net income as % of						
(i) Sales	8.2	5.9	8.5	4.6	5.0	2.5
Rank	65	159	58	257	219	399
(ii) Stockholders' equity	16.7	18.3	18.6	10.4	9.2	15.5
Rank	99	67	60	361	389	146
Earnings per share						
(i) 1966 ($)	3.44	0.94	0.77	2.95	2.76	1.44
1976 ($)	7.48	4.26	4.47	4.54	4.23	3.82
(ii) Growth rate (%) 1966-1976	8.08	16.31	19.23	4.41	4.36	10.25
Rank	221	43	27	320	322	156
Total return to investors (%)	15.05	17.18	18.54	25.69	22.03	71.67
Rank	366	357	342	297	321	84
1966-1976 average (%)	12.31	7.16	24.22	10.29	7.39	16.26
Rank	113	248	10	160	242	45

Source: The Fortune Directory of the 500 Largest United States Industrial Corporations, May 1970 and May 1977.

Note: Loews ranked 320 by sales in 1974, but is no longer treated by Fortune as an industrial corporation.

a/ Figures in brackets refer to the ranking in 1968. A dash (-) indicates a ranking in 1968 below 500.

b/ About 10 per cent of the equity is owned by Rembrandt/Rothmans Consortium.

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of which the first is a joint holding company of BAT and Imperial. In Brazil, BAT covers 85 per cent of the market, Reynolds 11 per cent and Philip Morris 5 per cent. Similarly, in Mexico it appears that "denationalization" of tobacco manufacturing is now almost complete. 19/

Table 6

Ranking a/ of selected tobacco transnational corporations among the 300 largest industrial corporations outside the United States, 1974

Business indicators	BAT b/	Imperial Group	Rothmans c/ International
Sales ($ million)	5 152	2 731	721
Rank	25	64	265
Assets ($ million)	4 507	3 136	1 030
Net income ($ million)	275	91	12
Stockholders' equity ($ million)	1 970	1 407	249
Employees	157 015	100 000	25 000

Source: Fortune, August 1975

a/ Ranked by sales.

b/ British American Tobacco ranks 49 by sales amongst the 50 largest corporations in the world.

c/ Refers to Rothmans International only and not to the Rembrandt Group.

D. Role of technology

34. The wellspring of what was to become a technological torrent of innovation after 1900 was the Bonsack cigarette machine patented in 1881 and producing 200 cigarettes per minute. The technological distance covered can be seen by the productivity of the Molins machine which, in 1976 was producing 5,000 cigarettes per minute (see table 7). BAT and Imperial have 50 per cent of the equity shares of the company.

19/ For a discussion of the concept of "denationalization" in Brazil and Mexico see United States Congress, Senate Committee on Foreign Relations, Report to the Subcommittee on Multinational Corporations (94th Congress, 1st session, August 1975) by R.S. Newfarmer and W.F. Mueller. In this context see also the study prepared for UNCTAD by J. Epstein and K. R. U. Mirow, "Impact on developing countries of restrictive business practices of transnational corporations in the electrical equipment industry: A case study of Brazil" (UNCTAD/ST/MD/9 and Corr.1).

Table 7

Cigarettes: Trends in machine output, 1881-1976

Manufacturer	Year	Model	Output per minute (number)
Bonsack	1881	Original	200
Bonsack	1899	Revised	500
Molins	1927	Mark I	1 000
Molins	1951	Mark 5	1 250
Molins	1955	Mark 6	1 600
Molins	1972	Mark 8	3 000
Molins	1976	Mark 9	5 000

Source: Trade sources.

[illegible]. Molin's technology and that of American Machines and Foundry, Hauni and other cigarette machine producers are marketed globally. Accordingly, the technological pacesetters of the industry have generated ever increasing economies of scale directly contributing to boosting the concentration of capital. United States capital invested per employee in manufacturing investment per production worker was $108,500 (see Chart V) (outpaced only by the petroleum industry covering extraction, refining and pipeline transportation), or more than twice the average for all manufacturing industry. Expressed in capital invested per worker, this represented a growth of 8 per cent annually between [illegible] and 1972.

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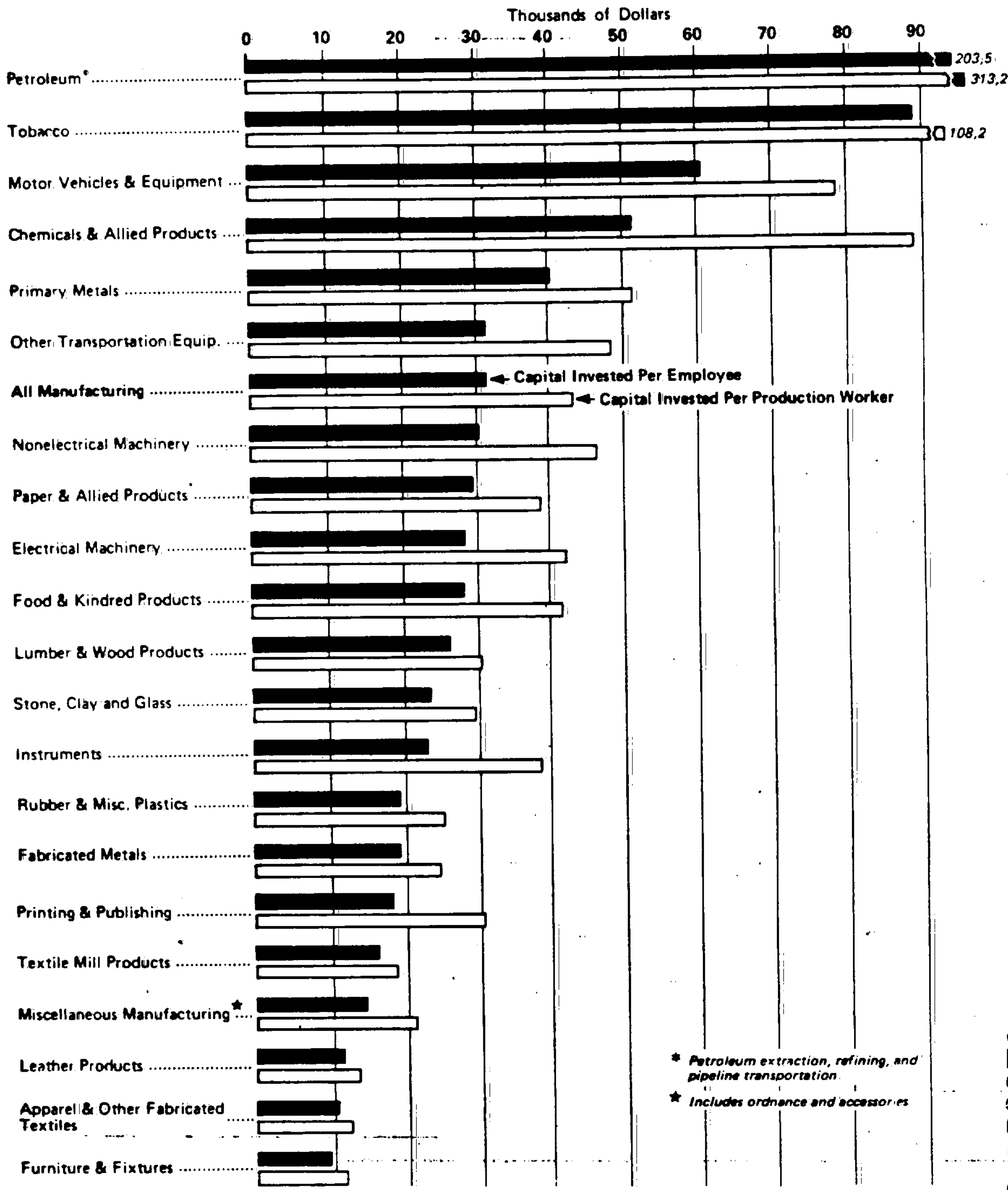
Chart V

UNITED STATES : CAPITAL INVESTED PER EMPLOYEE IN MANUFACTURING, 1972



Source : Data supplied to the UNCTAD secretariat by the Conference Board based on data of the United States Bureau of Labor Statistics and United States Internal Revenue Service.

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E. Finance capital

36. The expansionist momentum of the tobacco conglomerates was made possible not only by the specifically addictive nature of the commodity which has remained tax and depression-proof over the decades, but also by the intricate working relations that had been forged between finance capital and the industry on a global basis.

37. The TTCs, in their totality, cannot therefore be perceived as wholly separate entities from the larger banks, strikingly so in the case of the seven large New York banks or the British "Big Four". Recognition of this interdependence does not imply that the banks "control" the conglomerates in their managerial and marketing operations. Rather, it serves to pin-point the close and mutually beneficial co-operation in their operating relations, given the sheer profitability of the tobacco conglomerates.

38. The high level of sales turnover, together with the imperatives of expansion, contributes to making self-financing an economically unsound proposition. For the TTCs, moreover, one of the technical imperatives of the industry is that it requires tobacco stocks of 2 to 3 years' duration. Consequently, a sizeable proportion of the manufacturers' tangible assets are tied up in inventories.

39. The needs to utilize borrowed funds and to find non-tobacco uses for cash flow are co-existent, not contradictory. The TTCs seek leverage from borrowing at less than their internal rate of return to maximize surpluses accruing to the enterprise. Given the stability of their tobacco activities, and the ready marketability of their inventories to distributors, TTCs are in a nearly ideal position to maximize leverage with little risk to themselves.

40. It is widely recognized that the transnationals have harnessed domestic capital in the developing countries, notably in Latin America, to meet their business requirements. The same is true of Canada, whose four major banks have financed the operations of the TTCs. Local industry has often been taken over through the mediation of the transnational banking structure, as well as of purely national banks. This is so because, as Latin American experience shows, subsidiaries of the dominant conglomerates are able to obtain greater financial assistance from "national" financial institutions than can indigenous industrial corporations. Certain studies have revealed that between 1960 and 1970 about 78 per cent of manufacturing operations of United States corporations in Latin America were financed by domestic capital.20/ An estimated 90 per cent of the aggregate investments of TTCs in Latin America was financed by domestic capital siphoned through the transnational banking structure.

20/ Cf. the study by Fernando Fajnzylber, Estrategía industrial y empresas internacionales: Posición relativa de America Latina y Brazil, ECLA-IPEA, Rio de Janeiro, 1970. According to this author, foreign corporations financed about 85 per cent of their Latin American investment out of national funds, which offers an insight into the dimension of the transfer of resources, particularly when profit remittances are taken into consideration. For a comprehensive summary of the study see Economic Survey of Latin America 1970 (United Nations publication, Sales No. E.72.II.G.1).

41. Sri Lanka offers perhaps, the extreme example since, in the view of one observer, the Ceylon Tobacco Company (a BAT subsidiary), has not brought any foreign capital into that country since 1938.21/ Understandably, no systematic published data are available on BAT's profit repatriation from its Sri Lanka subsidiary before and after independence.

F. Cross-subsidization

42. The mechanics of cross-subsidization (which often assumes the superficial appearance of diversification), by which economic power in one sector is used to gain power over other sectors is one of the outstanding traits of all the TTCs, without exception.

43. Gulf and Western has now become one of the leaders in the United States apparel industry. It bought out the Kayser-Roth Corporation (which ranked number three in the industry, with annual sales reaching $545 million).22/ Cross-subsidization has induced a change in name of the General Cigar Co. to the Culbro Corporation, dictated by several takeovers after 1975, notably that of Helme Products with sales of around $100 million in snack foods and tobacco products. While still having a sizeable segment of the cigar market, it now extends its domain to proprietary medicine, plastics, land development and other sectors.23/

44. South Africa's Rembrandt Group, which owns or controls Rothmans International, Carreras, Brinkmann, Turmac, Tobacofina, Dunhill and the Liggett Group, to underline only the "tobacco" interests, has now embarked on extended diversification involving the acquisition of Federale Mynbou Beperk, with its interests in gold, uranium, coal and other minerals.24/ Such cross-subsidization is not, however, exclusively the prerogative of the parent company; it also takes place with the subsidiary, involving, once again, takeovers and mergers that have no apparent connexion with the "tobacco" industry.25/

21/ Fr. Tissa Balasuriya, "Our Multinationals", Ceylon Daily News, 25 March 1976. See also the same author's article "Ceylon Tobacco Co." in Logos, Vol. 15, No. 1, 1976.

22/ Forbes, 1 December 1976.

23/ Barron's, 14 June 1976.

24/ Tobacco Reporter, December 1976.

25/ **Rothmans International**'s aim is to bring down tobacco sales to less than 50 per cent of total sales. Cross-subsidization does not necessarily involve major cost purchases, but minor ones such as that of Simmons (a Burlington Arcade shop in Piccadilly, London) by Dunhill for $250,000. Likewise, Liggett's purchase of the Tetley Corporation, a beverage corporation, for $27 million, would boost the 57 per cent of revenue derived in 1975 from non-tobacco products.

45. Despite sustained cross-subsidization of R.J. Reynolds since the early 1960s, tobacco sales still account for 65 per cent of total business and provide (supplemented by corporate finance) the requisite resources for the growth of tobacco and non-tobacco enterprises. The $1.6 billion United States tobacco business, which provided $235 million profit net (or 14 per cent on sales), yielded as much as 23 per cent on invested capital. Larger and larger acquisitions in shipping, petroleum exploration, foods and beverages, packaging, etc. are now being actively sought. Sales springing from the Sealand takeover soared from $280 million in 1969 to over $854 million in 1974. Aminoil International, R.J. Reynolds' petroleum subsidiary, was acquired, it was claimed, to ensure Sealand's vessels an adequate fuel supply. Its oil revenues have rocketed from $10 million in 1970 to over $800 million in 1976, an 80-fold increase. To broaden further its petroleum base, the Burmah Oil Company (a Scottish Corporation) was bought for cash at a cost of $520 million. 26/

46. BAT, the world's biggest tobacco corporation, follows a similar cross-subsidization trajectory. Although it has diversified rapidly since 1970, with outlays of some $830 million, it has been able to achieve this build-up largely from profits reaped from tobacco, which still account for about three-quarters of its total profits.

47. It is this swift tempo of accumulation, from which the cross-subsidization mechanism has been fed, which made possible the recent take-over by BAT of the largest Swiss cosmetics corporation, Juvena, and some of the biggest department stores in the United States. Saks, Gimbels and the Kohl supermarket chain. The latter has its own network of more than 90 stores.

G. The role of advertising

48. The TTCs are in control of the three vital, interacting components of market power: industrial technology, finance capital and the sophisticated technology of consumer persuasion popularized under the designation of marketing techniques. This all-pervasive ideological control does not beguile consumers only in the developed countries; it has even greater potency in the developing countries. In certain developing countries, such as Brazil, several of the constraints imposed on advertising in developed market-economy countries do not exist, and use is made of media such as television which have been eliminated in most developed market-economy countries for tobacco advertising.

49. Corporate advertising, by its emphasis on selected brands, influences oligopolistic production and also reinforces capital concentration. In the United States, ten leading cigarette brands account for 74 per cent of consumption, and the first 20 for 91 per cent. Such brand concentration holds not only for the United States, but also for all countries and sectors where oligopolistic power is paramount.

50. The six majors in the 1950s marketed 16 brands of identical 70 mm length with uniformly high nicotine and tar contents; there are now 172 brands, of different lengths, with varying nicotine and tar contents. A large proportion of

26/ Wall Street Journal, 4 June 1976.

these are in test markets, as well as line extensions of existing brands. The extent of product differentiation in the United States (valid for TTCs' global operations as a whole) is illustrated by the fact that almost a third of current cigarette consumption is accounted for by some 60 new brands, or varieties of previous brands which were not on the market ten years ago.

51. This trend reflects non-price competition, where emphasis is on the withdrawal of unsuccessful brands and the launching of new ones, achieved by influencing consumers through the vast array of persuasion techniques, the so-called "hidden persuaders" which illustrate the ingenuity and the social waste of advertising.

52. In 1975, the cost estimated for launching a new brand of cigarettes in the United States market was $12-15 million in the first year. The launching of Philip Morris's "Merit" is indicative of the economies of scale in advertising. Marketing strategy demanded an outlay of $42 million - out of gross sales of $100 million - to launch that brand, corresponding to some 75-80 per cent of net earnings. Not to be outpaced in the low-tar 27/ brand race, R.J. Reynolds has financed a new brand, "Real", with a six-month's expenditure of $40 million, reported to be the most expensive outlay in the history of packaged goods.28/ Yet officially declared advertising outlays can be misleading. In the United States itself, where recorded media advertising is over $400 million per year for manufactured tobacco, actual advertising and promotion outlays are conservatively estimated at $1 billion. Total tobacco advertising by TTCs is of the order of $1.8 billion.

27/ The present battle over the low-tar, or high-filtration, cigarette market has major consequences for the further concentration and centralization of capital within the industry, which could lead to the elimination of one or two smaller members of the world tobacco oligopoly. In mid-197[illegible] low-tar brands accounted for 20 per cent of United States domestic sales, and the proportion has risen considerably since then. This means that any TTC has to be strong in the low-tar market to sustain profit margins. Hence, viewed from a marketing perspective, unless a TTC acquires a fairly sizeable segment of new smokers, its total market share will fall. In other words, the TTC that attracts the largest segment of the new smokers will attain the highest growth rate. A study of differential growth of the low-tar United States market is important for an analysis of market shares. At present, Reynolds has about 40 per cent of the market, with its "Now" and "Vantage" brands, and Philip Morris about 25 per cent, with the fastest-growing brand, "Merit". The fact that American Brands and Liggett have lost sizeable ground among smokers aged 25 years and below implies more than a loss in market power; in the medium and long run it could undermine their present market power, leading to a greater concentration in the major TTCs: Reynolds and Philip Morris.

28/ Business Week, 23 May 1977.

53. Formal corporate disclosure of advertising costs, as with transfer prices, is open to subtle and effective manipulative techniques. Moreover, the officially stated mass media advertising expenditures omit such vital data as commission fees to jobbers and advertising corporations. The vital importance of the need for such manipulation stems from the gains involved in the battle for ever greater unit volume and market aggrandizement: each 1 per cent gain, in the United States market share, is translated into $50 million net of Federal excise taxes.

H. The "pay-off complex"

54. In addition to mass advertising, another component of world tobacco marketing is global corporate bribery or the "pay-off complex", involving millions of dollars. Only a small fraction of these pay-offs has been uncovered in recent years - exclusively in the United States due to the increasing rigour of the investigative activities of the United States Securities and Exchange Commission (SEC).29/ The disclosures of Philip Morris in its 8K report filed with the Securities and Exchange Commission indicated that $2.4 million in "questionable payments" had been made by the parent company and its subsidiaries over the last five years.30/

55. Invariably, all the tobacco conglomerates, as most other corporations, have received a bonus from the "pay-off complex" by computing their profits on the basis of total costs, which are simply inflated to include bribes.31/ The mode of conduct of the TTCs has not been dissimilar to other corporate entities to whom the pay-off complex had become the conventional medium of the marketing and distribution mechanisms, joined to the enveloping secrecy and non-accountability that govern corporate practices.

29/ Over five years (1970-1975) R.J. Reynolds paid $19 million for illegal rebates (by its shipping subsidiary) to shippers, consignees and forwarding agents. In addition, it acknowledged that it had used $190,000 in corporate funds to promote United States Congressional and Presidential candidates between 1968 and 1973, an amount which was $100,000 more than it had originally disclosed to the SEC in May 1976. The accounting device employed to disguise the Congressional and Presidential contributions involved, according to the SEC, diverting a royalty payment due from a foreign licence and paying inaccurate invoices, purported to be from other foreign companies. Proceeds were placed in a cash fund and contributions despatched to candidates through representatives in the Company's Washington office (Wall Street Journal, 13 September 1976).

30/ According to the Wall Street Journal, 27 December 1976, the President of the Philip Morris affiliate declared that it hands pay-offs to all major political parties, but particularly to the dominant ruling party - "such pay-offs are necessary for corporate survival and profitability" and "pay-offs were essential to get favourable legislation enacted".

31/ Mintz, M. and Cohen, J.S. Power Inc.: Public and private rulers and how to make them accountable, New York, 1976, p.138.

I. Future prospects

56. There are major areas in which the global marketing strategies of the tobacco transnational conglomerates will continue to be focused in the immediate future: in the domain of technology, where increasing rationalization will serve to erode the market shares and the number of independent manufacturers in developing and the developed market-economy countries, and in the extension of cross-subsidization, which remains the main marketing and production strategy of the conglomerates.

57. These will be matched by accelerated concentration of the wholesaling and retailing sectors, with the industry becoming increasingly computerized. The strides in manufacturing concentration will also be seen in agriculture which has, until recently, resisted the encroachments of mechanization of the tobacco crop. Its momentum will increase rapidly in the late 1970s and 1980s, not only in the United States, but also in other leading producer countries.

58. Under the pressure for low-tar products and the desire to rationalize costs, a large array of "non-tobacco smoking materials" will be used as tobacco substitutes and extenders, bringing the "tobacco" industry into closer interaction with the giant oligopolies of the chemical industry. The above-mentioned technical variables and their interplay will, of course, influence tobacco marketing from the leaf stage to the final product.

59. The sheer dimension of the capital accumulation that has been unleashed calls for more effective regulatory control of the industry. Some inroads have been made in this direction in the developed market-economy countries, specifically in the United States, but few in the developing countries, where the global tobacco conglomerates operate under the protection of antiquated company legislation that effectively conceals the workings of corporate power.

60. The primary role of the TTCs in the marketing and distribution of tobacco leaf and manufactured tobacco indicates that the world tobacco economy continues to be dominated by these global corporations. Unless it is matched by effective countervailing power at the national level, the present play of forces must lead to further concentration, with all its implications.

Chapter II

THE ANATOMY OF CONTROL

A. The centre of power

61. The world tobacco economy has been fashioned by the dominance of a handful of TTCs and their deepening synchronization. At all stages of the production and marketing chain a handful of giant corporations, whose epicentres of power remain the United States and the United Kingdom, exercises decisive control. The "tobacco" industry, as epitomized by the TTCs, now straddles through cross-subsidization into almost the entire spectrum of modern industry, transportation, services and plantation agriculture.

62. The following industries reveal the ubiquity and variety of their cross-subsidizations: pulp and paper, paperboard, folding cartons, book matches, alcoholic and distilled beverages, department stores and supermarkets, cosmetics, toiletries, insurance and financial services, pipeline construction, refinery and chemical construction, textile chemicals, power generating equipment, marine construction, oil and gas drilling equipment, automotive/aviation spare parts, public safety control systems, industrial process control systems, metalworking presses, molded plastics, iron and steel castings, heat transfer components, construction and building products, dog food, raw and refined cane sugar, citrus and other fruits and vegetables, mining enterprises covering titanium, chrome, iron ore, uranium, coal, gold, platinum, asbestos, manganese, fluorspar and zinc, petroleum exploration, refining and marketing, breweries, food industry, optical goods and services, real estate, residential construction, cinema films, television activities, entertainment, records, textiles and apparel, watchmaking, proprietary drugs, etc.

63. The object of this chapter is to examine briefly the mechanics of the capital accumulation process within the individual TTCs and the impelling motives for, and extent of, this control.

64. While its global basis may be said to be oligopolistic in its marketing and distribution aspects, the industry is bound by technological and financial imperatives which lead to an overwhelming and ultimate concern with growth in sales volume. This growth is achieved through even larger market shares, as well as innovative breakthroughs (i.e. tobacco chemistry) and sustained high levels of productivity and its growth which have, up to the present, offset high capital costs. While there is competition within the global oligopoly, there is also collusion, which finds its reflection in interlocking directorates, cross-licensing and mutually supportive brands.

65. Of vital importance is that competition and collusion among the TTCs are not mutually exclusive but interacting. Collusion assumes many forms, such as the exchange and sale of trademarks, allocation of market spheres of influence, concerted action when their combined interests are thought to be jeopardized by national regulatory bodies, governments or rival trading interests. Competition is in the non-price field, where minimal gains in market shares are achieved as a result of highly intensive advertising and sales techniques.

B. Levels of concentration and corporate expansion

66. In relative terms the tobacco industry in the United States is one of the most highly concentrated of all manufacturing industries. According to four major ~~indicators,~~ namely sales, total assets, net capital assets and profits, the industry ranks second in terms of the shares accounted for by the leading industries - surpassed only by the motor vehicles industry.

67. The scale of operations of the leading seven TTCs can be seen from the figures relating to output of cigarettes on a global basis presented in table 8. These firms account for more than 39 per cent of world output, a share which rises to above 58 per cent if the socialist countries of Eastern Europe and Asia are excluded, and to nearly 80 per cent if both these countries and State monopoly countries are excluded. It should be emphasized that the shares are in actual fact higher, since brand shares of the oligopoly within the State monopolies, and to a lesser extent in the socialist countries of Eastern Europe are excluded.

68. An interesting feature is the extent of the concentration at the brand level. Within the United States, which is by far the largest market outside the socialist countries of Eastern Europe, four brands yield half of all sales (Winston, 15.4 per cent; Marlboro, 15.2 per cent; Kool, 10.3 per cent and Salem, 8.4 per cent).

69. It is no longer rational to discuss the activities of the TTCs as if their boundaries were confined exclusively to tobacco, or as if their organizational structure closely resembled that of firms in the sense in which that concept has commonly been construed. Although profits from tobacco sales still provide a crucial contribution to overall profits, all of today's TTCs derive a substantial and growing share of their aggregate returns from diverse efforts bearing but minimal connexions to tobacco. Thus, in 1973, close to one-half of the $11 billion sales recorded by the tobacco transnationals were from non-tobacco activities, which should be compared with the position at the end of the 1950s, when practically none of the sales of these corporations emanated from anything save tobacco. The recent acquisitions (1978) by BAT of the Appleton Paper Division (of the NCR Corporation) for $280 million cash and that of Seven-Up by Philip Morris for $515 million are merely illustrative of the conglomerate annexationist thrust of the engine of capital accumulation.

70. The outward spread of the corporations originally concentrating on tobacco has been far stronger than any inroads into the tobacco field by corporate giants with their centre of power in other areas. Hence, while the TTCs have succeeded in conserving part of the profits generated in different commercial activities, they have simultaneously succeeded in retaining tobacco profits within their control. However, the three relatively new members of the oligopoly exhibited the techniques of penetration. South Africa's Rembrandt group held a dominant position in an important secondary market and from it moved to take control over two of the weakest TTCs (Rothmans and Liggett and Myers). Loews, as an initial step in building up its conglomerate structure, acquired a weak TTC (Lorillard) which had suffered a sustained loss of market shares. Gulf and Western entered the less concentrated cigar market and eschewed cigarettes entirely. No new

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Table 8

Estimated world cigarette output by major groups, 1974

(in billions)

A State monopolies		%	B Socialist countries of Eastern Europe and Asia		%	C TTCs		%	D Others a/	%	E World Total	%
			I. Socialist countries of Eastern Europe									
Japan	292	7.9	USSR	369	10.0	BAT	500	13.6				
France	82	2.2	Other Eastern Europe	290	7.9	Philip Morris	274	7.5				
Italy	66	1.8				R.J. Reynolds	232	6.3				
Turkey	52	1.4				Rupert/ Rothmans	200	5.4				
Spain	36	1.0				Imperial (UK market)	108	2.9				
			II. Socialist countries of Asia b/									
Egypt	26	0.7		530	14.4	American Brands (US market)	95	2.6				
Cuba	23	0.6				American Brands (Gallaher UK market)	38	1.0				
Maghreb countries	23	0.6										
Thailand	21	0.6										
Austria	14	0.4										
Iran	12	0.3										
Sub-totals	647	17.6		1 189	32.3		1 447	39.4	1 447	10.7	3 676	100.0

Sources: United States Department of Agriculture, Foreign Agriculture Circular, FT5-75, December 1975, and speech by G. Collingwood, Vice-President and Financial Officer, Philip Morris, as published in Maxwell Consumer Services Reports: The Tobacco Conference, 5-11 June 1975; and UNCTAD secretariat estimates.

a/ Includes State monopolies and TTCs not listed, as well as independent domestic companies.

b/ Includes China, the former Democratic Republic of Viet-Nam and Democratic People's Republic of Korea.

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major cigarette manufacturer has started from scratch and no TTC which is financially solid and has a sound market-share has been taken over. Even a second-line TTC like Reemtsma has been immune to takeovers by maintaining reasonable surplus generating capacity and a special relationship with a major bank (Dresdener) to ward off unwelcome bids.

C. Banking linkages

71. Crucial to the growth of TTCs, as already mentioned in chapter I, has been their close linkages with large banks of which only fragmentary, but significant, indicators are available. The American TTCs are not only linked with the large American banks, but also with non-American finance capital. It is not fortuitous that the Chairmen of the Deutsche Bank and Mitsubishi are on the international advisory board of R.J. Reynolds. It is such financial leverage that permitted takeovers by Reynolds of an enterprise valued at $530 million and other, lesser, acquisitions within a short time span. Mr. Edmund L. de Rothschild is an institutional shareholder and a member of the Board of Directors of Rothmans International. 32/ In 1976, Mr. de Rothschild joined the Board of the Rembrandt Group. 33/ The connexions between Reemtsma of the Federal Republic of Germany (with 37.4 per cent of the market of that country and 25 per cent of the Argentine market) and the Deutsche Bank are of 40 years' standing. This close interconnexion between industrial and finance capital and consequent economic concentration is best expressed in the words of an executive officer of the Dresdener Bank: "It is banks who are in the best position to decide the question of mergers", 34/ i.e. the restructuring of industry and marketing channels.

D. Globalization of output

72. Globalization of output and sales, the second path of expansion, has likewise been a feature of the post-1960 period. Within the United States the growth potential has been exiguous. Outside, however, the world market (excluding the socialist countries of Eastern Europe) was, in 1974, about three times the size of the United States market and was growing twice as fast. True, there had always been the possibility of exporting to meet foreign demand. However, the constraints imposed by trade and tariff barriers, particularly in the European Economic Community (EEC), and growing recognition of the advantages to be derived from lower local costs of production abroad and (probably of much greater significance) the importance of being close to the consumer in a product where so much depends on accurately gearing advertising to local conditions, have made foreign production appear more attractive than exporting.

73. Table 9 shows market shares for cigarettes of selected TTCs and/or companies related to them in 30 countries in 1975 or for the most recently available earlier year. In only a few of the countries distinguished did producers other than those

32/ Annual Reports and Accounts, 1975. Likewise, Lord Pritchard, Chairman of Rothmans International, is a director of two of the leading United Kingdom finance houses, Midland Bank and Samuel Montagu. (Tobacco Reporter, March 1977).

33/ A. Rupert, Partners in Progress, Rembrandt Group Ltd., Stellenbosch 1976, p. 10.

34/ "Three Rich Powerful Banks Dominate the Economy", Business Week, 19 April 1976.

Table 9

Cigarettes: market shares a/ of selected TTCs and affiliates, 1975
(in per cent)

Country	American Brands	BAT %	Liggett & Myers %	Philip Morris %	R.J. Reynolds %	Rupert/Rothman's Group %	Others b/	Total Sales (million pieces)
Argentina		Nobleza 37	Picardo 18	Massalin 16			29 c/	38,200
Australia		Wills 36		PM 30		Rothmans Australia 26	8	31,300
Belgium		Warland 12		Weltab 6		Tabacofina 46	36 c/	18,900
Brazil(1974)		Souza Cruz 75		PM 5	d/		20	100,300
Canada		Imasco e/ 42		Benson & Hedges 11	Macdonald 18	Rothmans of Pall Mall (Canada) 22	7	57,900
Costa Rica		Republic Tobacco Co. 57		Tabacalera Costarricanse 16			27	2,200
Denmark							f/	7,100
El Salvador		Morazan 76		Centro-americana 15			9	2,099
Finland		Suomen Tupakka 27					73	8,100
Germany, Fed Rep. of		BAT Cigaretten Fabr. 25		PM 6	Neuerburg 5	Martin Brinkmann 19	45 c/	123,900
Ghana(1974)		Pioneer 100						...
Guatemala				Centro-americana 47			53	2,300
India		ITC Ltd. 37 VazirSultan 24		Godfrey Phillips 5			34	60,800 (1974)
Jamaica		Machada 27				Carreras 68	5	1,540
Kenya		BAT(Kenya) 100						3,300 (1974)
Malaysia(1971)		Malayan Tob. Co. 66				Rothmans of Pall Mall(Malaysia)17	17	8,966
Mexico		La Moderna 30		Tabacalera Mexicana 14			56	45,300
Netherlands	Niemeyer g/ 12	BAT (Netherland)23		PM Holland 3		Turmac 17 Laurens 29 Gruno 1	15	23,900
New Zealand		Wills 16		PM New Zealand 6		Rothmans 70	8	5,900
Nicaragua		Tabacalera Nicaraguese 96					4	...
Nigeria		Nigerian Tob. Co. 66		PM Nigeria 12			22	11,330
Pakistan		Pakistan Tob. Co. 35		Premier Tob. Co. 28			37	25,800
Panama		Tabacalera Istmena 55		Tabacalera Nacional 43			2	1,005
Peru (1973)			Tabacalera Valor h/ 14				86	3,488
Sri Lanka		Ceylon Tob. Co. 100						...
Switzerland		BAT (Suisse)15		Fab. de Tabacs Réunies 26	Reynolds Cig. Corp. 1	Laurens (Rothmans) 5	53	26,700
United Kingdom	Gallaher 26					Carreras 6	68 i/	132,000
United States	American Tobacco 15	Brown & Williamson 17	4	23	32		9 j/	599,410
Venezuela		Bigott Sues 19		Tabacalera Nacional 76			5	16,700
Zaire(1974)		BAT Zaire 28					72 k/	5,000
Zambia(1974)		Cigarette Man. Ltd. l/				Cigarette Man. Ltd. l/		...

Source: UNCTAD Secretariat calculations based on Maxwell's estimated brand shares and other trade sources.
a/ Includes cigarettes produced under licensing agreements.
b/ These may include small shares of brands produced by the listed TTCs
c/ Reemtsma (Germany, Fed. Rep.): Argentina 19 per cent, Belgium 14 per cent, Germany, Fed. Rep. 35 per cent.
d/ In 1975, RJR bought up Lopes S.A. which held 11 per cent of the market.
e/ Holding Co. of BAT (44 per cent) and Imperial (56 per cent).
f/ Scandinavian Tobacco Co. (BAT 31.3 per cent) is the sole cigarette producer.
g/ Through Gallaher.
h/ In 1975, Tabacalera Valor joined Tabacalera Nacional, a privately-owned company which, in 1975, held 57 per cent of the market.
i/ Imperial: 64 per cent.
j/ Lorillard: 7 per cent
k/ Tabazaire.
l/ Jointly-owned by BAT (30 per cent) and Rothman's (70 per cent) is the only cigarette manufacturer.

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affiliated with the key corporations mentioned in the table reach 40 per cent or more of local sales. However, it is likely that some "local" producers are financially interrelated with members of the tobacco oligopoly, although this cannot be ascertained from company annual reports.

74. For the TTCs, as for others, entry into local markets has come through one or more of three well-known channels (with each of the channels sometimes being used sequentially):

- affiliation with, and ultimately acquisition of, domestic producing or advertising enterprises;
- spawning of subsidiaries.

75. The nature and importance of these channels vary among different members of the TTCs. Two flow charts are presented in the annex; the first (chart A) illustrates the financial interests of the United States-based TTCs on the one hand and the United Kingdom-based ones on the other, while the second (chart B) shows the licensing agreements, again separately for the United States and United Kingdom-based firms. They list the most important subsidiaries of the oligopoly and exhibit their interrelationships with companies in various countries (grouped by major world regions). However, the charts do not indicate whether the domestic companies, which in most cases have national names, are fully or partially owned subsidiaries or affiliates.

76. The flow charts on licensing agreements indicate the companies with which the seven United States majors have licensing agreements; for Europe, 10 companies and two State monopolies (Austria and France) have licensing agreements in a more restricted geographic area than United States companies. Details of licensing agreements on individual brands are not given because of the large number involved.

E. The tobacco transnational conglomerates (TTCs): Case histories

1. R.J. Reynolds Industries, Inc. (RJR)

77. In 1970, a new parent company, R.J. Reynolds Industries, was created, with the Reynolds Tobacco Company becoming a fully-owned subsidiary. The new company was not "a sign of decreasing interest in our tobacco enterprises. Rather, it is a sign that our diverse subsidiary interests have matured to the stage where they stand as fully-fledged members along with tobacco." 35/ Establishment of this affiliate gave formal recognition to the movement, initiated in 1956, aimed at facilitating investment in non-tobacco enterprises, the results of which may be seen from chart VI, which shows the corporate structure.

78. This compulsion to diversify was dictated by the mechanics of the firm's internal capital accumulation. "First, having captured one-third of the United States cigarette market, the company could see a point of diminishing returns for growth potential. Second, significant cash was being generated which could be invested advantageously elsewhere." 36/ Adopting "an unrestricted approach towards diversification", the company notes, "Reynolds moved into entire new areas - shipping and petroleum, on the theory that it made sense, when appropriate, to apply cash to any strong, well-established business." 37/

35/ R.J. Reynolds, Our 100th Anniversary, 1875-1975, Winston-Salem, North Carolina, 1975.

36/ Ibid. For the unfolding of this process see Nannie Tilley (op.cit.) in the official (mimeographed) listing of the Reynolds corporations.

37/ Ibid.

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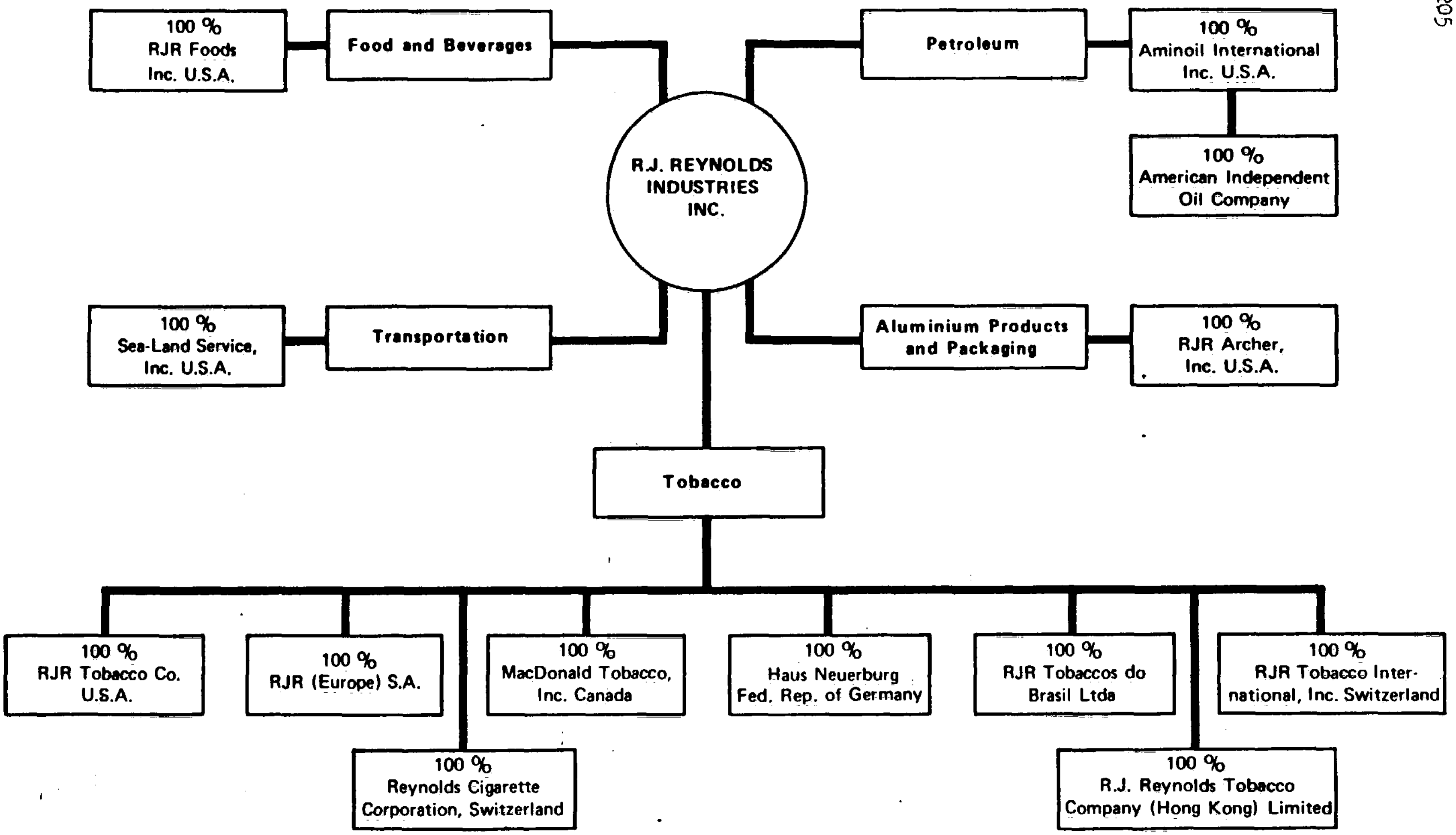
Chart VI

MAJOR BUSINESS GROUPS OF R.J. REYNOLDS INDUSTRIES, INC. U S A



SOURCE : *Compiled from data in S.E.C. 10-K Form, 1975.*

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Table 10

R. J. Reynolds Industries Inc. USA: Net sales and revenues and earnings from operations by major product lines, 1971-1975

Product line	1971	1972	1973	1974	1975
	Net sales and revenues (per cent)				
Tobacco	74.8	73.3	71.3	64.3	68.6
Transportation	12.9	15.2	17.7	19.0	15.9
Petroleum	2.6	2.7	3.0	10.3	9.1
Other	9.7	8.8	8.0	6.4	6.4
	100.0	100.0	100.0	100.0	100.0
	Earnings from operations (per cent)				
Tobacco	87.7	82.8	82.6	50.0	62.7
Petroleum	5.0	7.3	9.9	30.8	23.1
Transportation	3.5	6.5	3.3	17.3	10.6
Other	3.8	3.4	4.2	1.9	3.6
	100.0	100.0	100.0	100.0	100.0

Source: Company data.

79. Tobacco, maritime containerized transport, petroleum, aluminium and foods are the five basic industries accounting for almost all of the $4,500 million in sales and revenues in 1975, tobacco being the leader with 69 per cent (see chart VII). As may be seen from table 10, sales and revenues of its non-tobacco operations have climbed from 25 per cent of consolidated sales and revenues in 1971 to 31 per cent in 1975; and earnings from non-tobacco operations from 12 per cent to 37 per cent.

(a) Tobacco

80. The unfolding of successive phases of market penetration can be traced to the early 1960s with the acquisition of Haus Neuerburg, 38/ one of the leading cigarette producers in the Federal Republic of Germany. Systematic acquisition of foreign enterprises led to the setting up of R. J. Reynolds (Europe) as a subsidiary operating within the framework of EEC and the European Free Trade Association (EFTA), as well as for managing corporate interests in Africa and the Middle East.

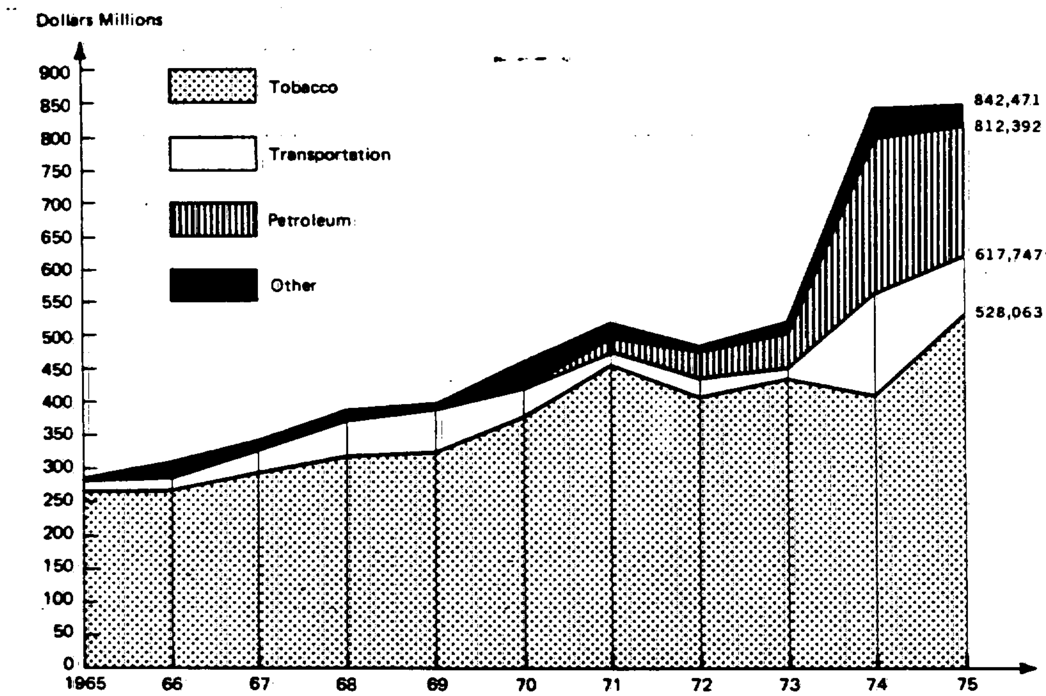
38/ The name has now been changed to R. J. Reynolds GmbH.

Chart VII

R. J. REYNOLDS INDUSTRIES, INC., USA

EARNINGS FROM OPERATIONS

(1965 – 1975)



SOURCE : R.J. Reynolds Industries Inc. 1974 and 1975 Annual Report.

81. In 1972, with the further growth of international operations, a new market reorganization was deemed necessary, resulting in the genesis of the Geneva-based R. J. Reynolds Tobacco International S.A., with regional extensions in Hong Kong, Rio de Janeiro and Beirut. With the present stress on greater centralization of decision-making, a new subsidiary, R. J. Reynolds Tobacco Company International Inc., now has its headquarters in Winston-Salem, North Carolina which remains the decisional power centre of Reynolds Industries. This finds its institutional expression in four major "areas" of penetration:

Area 1: Europe, Middle East and Africa

Area 2: Canada

Area 3: Brazil, Ecuador, Peru and Mexico

Area 4: Asia/Pacific

82. In 1970, the Macdonald Tobacco Co. of Canada, a manufacturer and distributer of cigarettes (with 22 per cent of the Canadian market), became the exclusive Canadian distributor of RJR cigarette brands. In 1974, it became a wholly-owned subsidiary at a stated price of $75 million. 39/ The Simon Cigar Co., Canada's second largest cigar manufacturer, was annexed by Macdonalds and became a wholly-owned subsidiary of Reynolds.

83. In 1974 RJR penetrated the Brazilian market by forming R. J. Reynolds Tobacos do Brazil Ltds. Through this subsidiary, in late 1975 it acquired the manufacturing and distribution assets of Cia. Lopes SA Industrial de Fumos, at a price exceeding $10 million. Lopes provided Reynolds with 11 per cent of the Brazilian market and an annual sales volume of approximately 8 billion units.

84. Although its corporate takeover was most marked in the Americas (Canada, Curaçao, Brazil, Ecuador) successful penetration also occurred in the Far East - in Indonesia and in Malaysia (where it bought a manufacturing plant from Gallaher), in Hong King, where it boosted its operational activities, and in Australia, where it absorbed its distributor. Within a five-year period the global cost of these acquisitions was estimated at $660 million.

(b) Convenience food and beverages

85. With the first non-tobacco acquisition in convenience food and beverages, its production operations entered new geographical areas. 40/ Already in the march to vertical integration of the 1920s, Reynolds set up its own foil division, "primarily to avoid reliance upon outside suppliers". 41/ Originally formed as a division of Reynolds to supply packaging materials for its tobacco

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39/ R. J. Reynolds, Annual Report, 1974.

40/ It now has 14 plants in 10 states of the United States and 2 Canadian provinces.

41/ Our 100th Anniversary, op. cit. In line with its policy of vertical integration, it was instrumental in building up a rival source of cigarette paper which conventionally had been produced only in France.

products, R. J. R. Archer Inc. became a fully-owned subsidiary in 1966. It is one of the United States leading suppliers of specialized foil and sheet aluminium. 42/

(c) Shipping

86. In order for Reynolds to break into the world shipping market for tobacco, estimated at around $85-$90 billion yearly, the world's largest containerized freight operations - the Sea Land Service (and the innovator of this revolutionary mode of transportation) - was taken over at a cost of $530 million, 43/ when Maclean Industries Inc. was dovetailed into Reynolds. Its share of the Atlantic and Pacific shipping market is now over 10 per cent. Expenditures on the transportation network exceeded $1 billion over a seven-year period by the end of 1975, 44/ involving the acquisition and construction of new vessels, containers, etc. A move to take over another containership corporation was blocked by the United States Justice Department.

(d) Petroleum

87. The next takeover was a logical follow-up of the first. After acquiring Sea Land it absorbred in 1970 the American Independent Oil Co. (Aminoil) an independent petroleum producer and refiner, in a move allegedly geared to meet the full demands of its fleet. Its main source of fuel oil, thus far, has been the Dividend Zone, an area of 2,560 square miles between Kuwait and Saudi Arabia and Iran, where it participates in the Iranian consortium.

88. In 1975, Aminoil's shipments of petroleum products from Kuwait averaged 72,000 barrels daily. In Kuwait Aminoil owns and operates an oil refinery, a desulphurization plant and related facilities. In addition to these countries, onshore and offshore explorations are under way on the Atlantic and Pacific Coasts and the Gulf of Alaska, the Gulf of Mexico, the North Sea, Paraguay, Guatemala, Spain and Indonesia. Petroleum remain one of the key profit sources with petroleum earnings jumping from 10 per cent to 31 per cent of total sales in one year from 1973 to 1974, in part due to the quadrupling of petroleum prices in that period.

2. The British American Tobacco Company (BAT)

89. The British American Tobacco Company (BAT) was brought into existence in September 1902 as a result of an agreement between the American Tobacco Company (ATC) and the Imperial Tobacco Company (ITC) for what was, in effect, a division of the world market whereby the two companies would exercise the rights to each others' brands in their agreed spheres of influence. BAT (in which Imperial acquired one-third and ATC two-thirds of the equity capital) became the sole exporting agency of ATC and Imperial, with the right to buy any export enterprise acquired by either of the two companies. Neither the United Kingdom nor the United States markets were to be within BAT's operational ambit.

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42/ In 1970 a merger movement was entered into with Walter Kidde and Company Inc. and United States Lines, Inc. under which Reynolds was to acquire all of the common stock of United States Lines in exchange for a $65 million promissory note payable to Kidde.

43/ Source: Company data.

44/ Source: Company data.

90. BAT, with total sales of over £5.4 billion ($9.2 billion) in 1976, ranks among the world's 50 largest corporations and as the third largest British industrial company. It is the world's leading tobacco company by sales, assets and number of employees. Whereas the primary corporate concern of the company and its subsidiaries is in tobacco manufacturing, it has also diversified considerably both in the years between the world wars and since 1950.

91. It has now extended its sizeable interests to various facets of retailing and distribution, paper and cosmetics. There are four major divisions of BAT's principal activities: tobacco, retailing, paper and cosmetics (see chart VIII). Another important business segment is included in the designation "other activities" and includes medium and short-term investment of financial resources, insurance and certain subsidiaries in the food industry.

(a) Tobacco

92. According to company data the overseas companies of the Tobacco Division operate 90 factories supplying domestic markets in 37 countries, and its affiliated companies operate 38 factories in 14 countries. 45/ Because of the conditions of its establishment more than 95 per cent of the Group's tobacco products are manufactured abroad, a situation which is now likely to change. It is claimed that in 40 of the countries supplied the dominant cigarette brand is a BAT product. BAT remains one of the world's major leaf exporters, with its annual United States exports accounting (through its wholly-owned subsidiary, the Export Leaf Tobacco Co.) for about $260 million. In Brazil, it is reported that BAT markets more than 80 per cent of the country's leaf exports.

93. When the two companies (ATC and ITC) alleged that the spheres of influence agreement referred to above had been formally terminated in 1972, they decided, in the words of the BAT chairman, that they intended by "all legal means, to arrange our affairs so that we don't compete with each other with identical brands in the same market". 46/ In addition to such market sharing, the two continue to enjoy intimate corporate relationships, as seen in Imasco in Canada, the Molins machine company and Mardon's International.

94. BAT's recent merger with the Tobacco Securities Trust (originally created in 1928 by BAT), an associated investment company, is a move designed to restructure itself on a holding company basis. Technically, the scheme has been structured as a merger by reverse takeover of BAT by Tobacco Securities. As a holding company for BAT, it will be renamed BAT Industries, 47/ and its board will be composed entirely of BAT's present directors. Since Tobacco Securities' assets included a substantial portfolio of tobacco investments, some of which

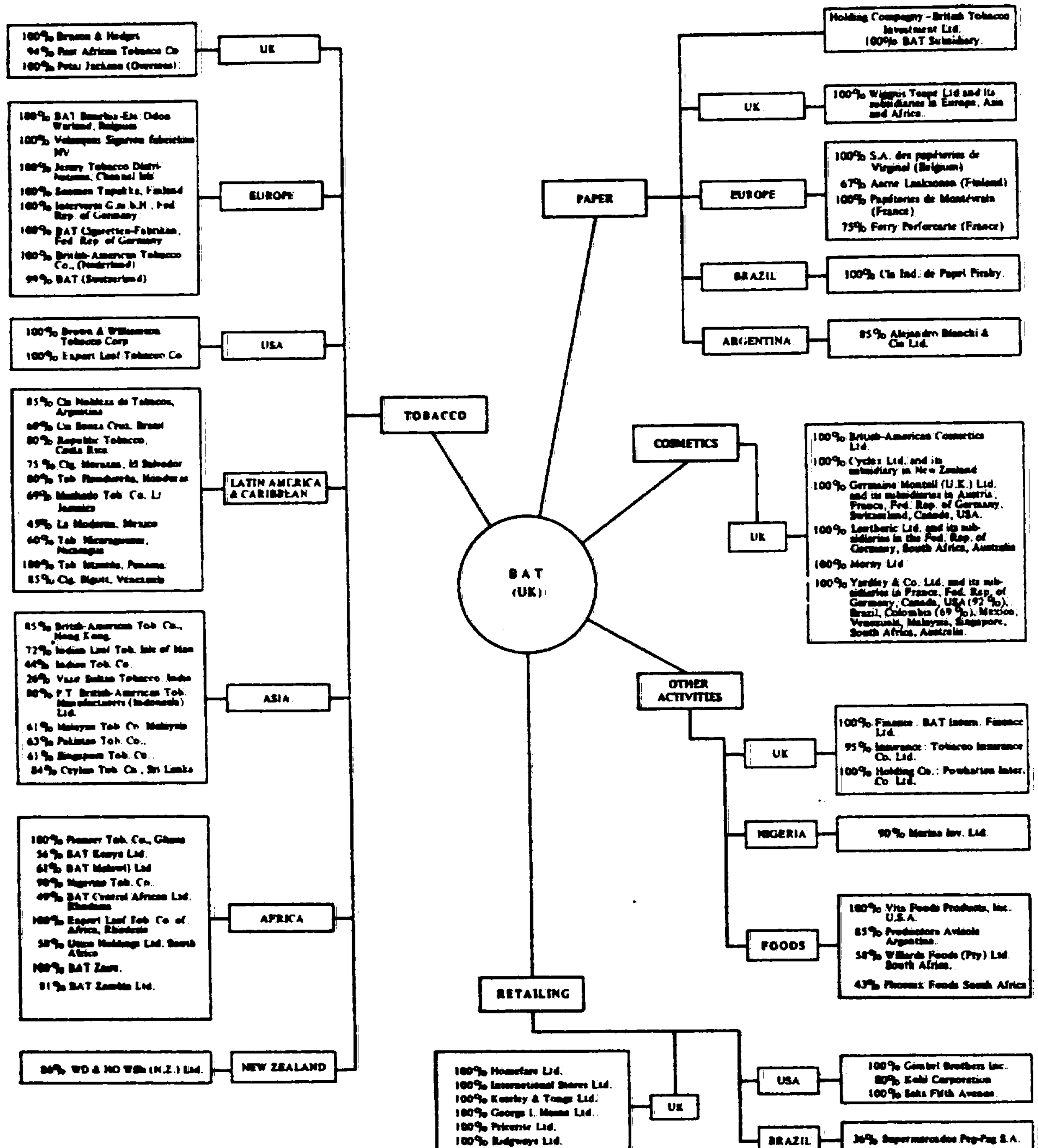
45/ BAT, Report and Accounts, 1976.

46/ Wall Street Journal, 17 August 1972.

47/ Imperial has a 22 per cent stake in Tobacco Securities, compared to BAT's 23 per cent, and is now prepared to divest itself of some of the holdings to BAT industries.

Chart VIII

MAJOR BUSINESS GROUPS OF BRITISH AMERICAN TOBACCO Co. Ltd.



SOURCE. Compiled from data in Report and Accounts, 1975.

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represented minority interests in BAT companies, the merger will bring all of these companies under BAT's direct control. 48/ In the immediate future it is therefore to be expected that BAT's shares in global marketing will rise. Tobacco manufacturing and leaf tobacco trading continue to be of paramount importance, with manufacturing accounting for 66 per cent and retailing for 23 per cent of turnover in 1976. In terms of operating profits, however, tobacco accounted for 75 per cent, whereas retailing provided only 8 per cent (see table 12).

95. A geographical analysis of turnover and operating profit indicates that the metropolitan market accounted in 1976 for 12 per cent of turnover and 10 per cent of operating profits, the major profit centres being North and South America (see table 11).

Table 11

BAT: Geographical analysis of turnover and operating profit structure, 1976

	Turnover		Operating profits	
	£ million	%	£ million	%
United States and Canada	1 778	31	171	40
Europe	1 365	24	68	16
Latin America	1 258	22	87	20
United Kingdom	656	12	45	10
Asia	326	6	33	8
Africa	220	4	20	5
Australasia	34	1	6	1
	5 637	100	430	100

Source: BAT Report and Accounts, 1976.

Table 12

BAT: Industrial analysis of turnover and operating profit structure, 1976

	Turnover		Operating profits	
	£ million	%	£ million	%
Tobacco	3 752	66	324	75
Retail	1 282	23	33	8
Paper	457	8	34	8
Cosmetics	91	2	5	1
Other activities	55	1	34	8
	5 637	100	430	100

Source: BAT Report and Accounts, 1976.

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48/ Financial Times, 1 May 1976.

96. At present the third largest cigarette manufacturer in the United States is Brown and Williamson Tobacco Corporation. With a market share of 16.5 per cent in 1975, it is a wholly-owned subsidiary which neither issues an annual report nor releases sales figures. However, according to trade estimates (based on cigarette unit sales) total sales in 1975 amounted to $1.5 billion. 49/

(b) Retailing

97. BAT has been in retailing and wholesaling for a considerable time. Its International Stores, F. J. Wallis and Pricerite together have over 1,000 supermarkets and self-service stores in England and Wales. It now accounts for 4-5 per cent of the United Kingdom retail grocery market. In the United States, Gimbel Brothers and Saks Fifth Avenue have respectively 38 general department and 30 high fashion stores in major metropolitan and suburban areas. The Kohl Corporation has 92 supermarkets and other retail stores in Wisconsin and Illinois. In the Federal Republic of Germany, BAT has a 25 per cent holding in Horten, which has 57 department stores. In Brazil it has acquired the Supermercados Peg Pag, which has 39 supermarkets in and around Sao Paulo and Rio de Janiero.

(c) Paper

98. Mardon Packaging International continues to be jointly owned by BAT and Imperial and produces a wide variety of packaging and paper materials in the United Kingdom, Europe and Canada. Wiggins Teape, a fully-owned subsidiary, is a producer of an extensive range of specialty and industrial papers, as well as of high-grade printing and writing papers. This subsidiary has 17 plants in the United Kingdom and others in Belgium, France, Ireland, Latin America, Africa and Asia, and is the largest United Kingdom exporter of paper products. In 1974, it acquired the outstanding 50 per cent interest held by The Mead Corporation of the United States in a Belgian joint venture, Papeteries de Virginal SA.

(d) Cosmetics

99. BAT's perfumery, cosmetics, toiletries and skin care products are manufactured in 38 countries. In 1976, BAT acquired one of the largest Swiss cosmetic transnational enterprises, Juvena with its product lines in Switzerland, the Federal Republic of Germany and Australia.

3. Imperial Group Ltd.

100. The Imperial Group is the sixth largest industrial company in the United Kingdom. 50/ Until 1972, the Group's tobacco division's activities were concentrated in that country in conformity with the spheres of influence agreements with BAT. Until very recently, it held about 30 per cent of BAT stock, but its share has now fallen to around 16 per cent. The Imperial Group's total sales were around £3 billion in 1976, or about 4 per cent of total consumer expenditure in the United Kingdom. Its share of the United Kingdom tobacco market was around 64 per cent in 1975. The major business divisions of Imperial are shown in chart IX.

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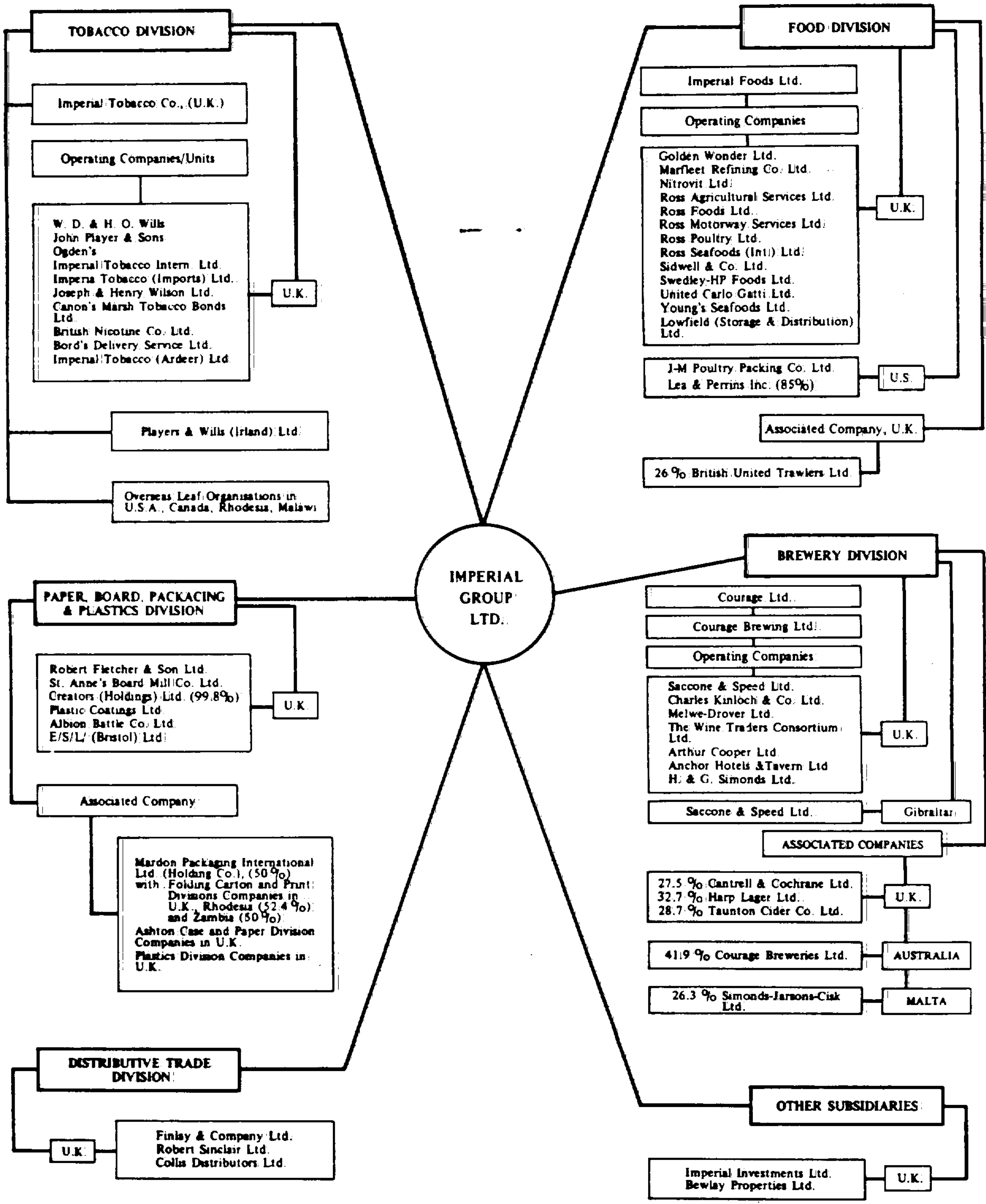
49/ Advertising Age, 23 August 1976.

50/ The Times, 1,000 Leading Companies in Britain and Overseas, 1974-1975, London 1976

Chart IX

MAJOR BUSINESS DIVISIONS OF IMPERIAL GROUP Ltd.



SOURCE : Compiled from Imperial Group Limited Report and Accounts 1975

(a) Tobacco

101. In the tobacco division Wills and Player focus mainly on cigarettes and Ogden's on other tobacco products. Although no data are available on tobacco sales by product line, it is estimated that around 90 per cent of total sales are in cigarettes, with pipe tobacco, cigars and hand-rolling tobaccos accounting for the remainder. New marketing possibilities for low-tar cigarettes appear to be opening up with the advent of new smoking materials in which two leading corporate entities - Imperial Chemical Industries and Imperial Tobacco Company - will be operating together.

(b) Food and beverages

102. As with the other tobacco conglomerates BAT is now rapidly diversifying into food and beverages. Its largest acquisition, the United Kingdom Courage brewing group in 1972, 51/ was a significant step into retailing as well as brewing and wholesaling. Over four-fifths of this group's profits came from pub outlets as well as other sales of wines and beer. Accounting for one-fifth of total sales, the Food Division is Imperial's second major profit centre and a rapidly growing one. Golden Wonder, a crisp manufacturer, was acquired in 1960, HP Sauce in 1967, followed in rapid succession by National Canning, the Ross Group and Allied Farm Group. The Imperial Group's canned foods are marketed under the Smedley label and the HP Sauce Division through the Lee and Perrins label, while Golden Wonder, which was a very minor marketing operation, has become a dominant national force in the industry.

103. The six major manufacturing divisions include poultry, poultry breeding and eggs, frozen foods, fish, potato crisps, sauces and other varied product lines. Its penetration of the United Kingdom catering trade, which began prior to World War I, appears to have slackened, which is commercially understandable in view of its already strong grip on the distributive trade.

(c) Overseas expansion

104. At present, Imperial's major marketing push is directed to Western Europe, following a change in policy by which BAT and Imperial ostensibly pursue separate development paths to conform with EEC competition rules. In mid-1973, Imperial established the Imperial Tobacco International Ltd. as the major marketing organization for its penetration outside the United Kingdom and Ireland. Already, marketing divisions have been opened in Denmark, Switzerland, the Federal Republic of Germany and Italy. More recently, continuing its further penetration of continental markets, Imperial has set up a second company in Switzerland (Imperial Tobacco Trading) to pursue its marketing interests in Italy, since under the legal terms of the State monopoly in that country it is prevented from setting up a manufacturing plant. A divisional analysis of sales by Imperial is given in table 13 below.

51/ Financial Times, 15 October 1975.

Table 13

Imperial: Sales analysis by major divisions, 1974-1976

(£ million)

Divisions	1974	%	1975	%	1976	%
Tobacco	1 111.7	56.7	1 400.9	57.3	1 654.7	55.8
Food	389.3	19.9	495.4	20.3	655.7	22.1
Brewery	236.6	12.1	298.2	12.2	369.3	12.4
Paper, board, packaging and plastics	115.4	5.9	128.3	5.2	159.9	5.4
Distributive trade	106.1	5.4	120.6	4.9	126.5	4.3
Total	1 959.1	100.0	2 443.4	100.0	2 966.1	100.0

Source: Imperial Group; Report and Accounts, 1975 and 1976.

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